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In The

Supreme Court of the United States

October Term, 1990

DONALD E. WILLIAMS, COMMISSIONER OF THE DEPARTMENT OF MOTOR VEHICLES, COMMONWEALTH OF VIRGINIA,
and
VIRGINIA AUTOMOBILE DEALERS ASSOCIATION, INC.,

Petitioners,

v.

SATURN DISTRIBUTION CORPORATION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

1. Does the Federal Arbitration Act apply to a state statute concerning contract formation?

2. Is there an "actual conflict" between the Federal Arbitration Act and a state statute of contract formation warranting preemption of the latter under the Supremacy Clause when the state statute ensures only that parties voluntarily enter into agreements containing forum selection clauses and does not affect the enforceability of existing arbitration agreements?

3. Can a state law of contract formation be construed as "singling out" arbitration for special treatment and unreasonably burdening parties' ability to enter into arbitration agreements where the statute applies to all forum selection clauses and requires only that parties voluntarily enter into arbitration agreements?

4. Does the Federal Arbitration Act allow automobile manufacturers/distributors to force their dealers to accept arbitration clauses as part of their franchise agreements when the Dealer's Day in Court Act specifically provides dealers access to federal courts to seek redress against manufacturers/distributors?

5. Did the panel majority in this case err in refusing to reconcile the Federal Arbitration Act, which mandates enforcement of arbitration agreements, and Virginia's interest in enforcing its automobile franchise laws, which require only that parties voluntarily enter into agreements containing forum selection clauses?

LIST OF ALL PARTIES

The petitioners, who were defendants in the action below, are Donald E. Williams, in his official capacity as Commissioner of the Department of Motor Vehicles of the Commonwealth of Virginia, and Virginia Automobile Dealers Association, Inc. The respondent, which was plaintiff in the action below, is Saturn Distribution Corporation, a wholly-owned subsidiary of Saturn Corporation. Saturn Corporation, in turn, is a wholly-owned subsidiary of General Motors Corporation.

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SATURN DISTRIBUTION CORPORATION,

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

Donald E. Williams, Commissioner of the Department of Motor Vehicles of the Commonwealth of Virginia (the "Commissioner"), and the Virginia Automobile Dealers Association, Inc. ("VADA"), respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fourth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1) is reported at 905 F.2d 719. The opinion of the district court

(Pet. App. 28) reversed by the court of appeals is reported at 717 F. Supp. 1147.

JURISDICTION

The court of appeals entered judgment on June 6, 1990. Pet. App. 1. On July 20, 1990, a petition for panel rehearing and a suggestion of rehearing in banc was denied. Pet. App. 43. This Court has jurisdiction under 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISION AND STATUTES INVOLVED

The pertinent parts of the following are reprinted as indicated: the Supremacy Clause, U.S. Const. art. VI, cl. 2 at Pet. App. 45; the Federal Arbitration Act, as amended, 9 U.S.C. §§ 1-13, at Pet. App. 46; the Dealer's Day in Court Act, as amended, 15 U.S.C. §§ 1221-1225, at Pet. App. 47-48; *Va. Code* § 46.1-550.5:24 at Pet. App. 49; and *Va. Code* § 46.1-550.5:27 at Pet. App. 50.

STATEMENT OF THE CASE

Respondent brought suit alleging that *Va. Code* §§ 46.1-550.5:24 and 46.1-550.5:27 were preempted by the Federal Arbitration Act ("FAA" or the "Act"), 9 U.S.C. §§ 1-13, under the Supremacy Clause of the United States Constitution.[1] The district court rejected this constitutional challenge. A divided court of appeals reversed, finding that § 46.1-550.5:27, but not § 46.1-550.5:24, was preempted by the FAA.

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[1] Title 46.1 of the Code of Virginia was repealed and §§ 46.1-550.5:24 and 46.1-550.5:27 were recodified as *Va. Code* §§ 46.2-1566 and 46.2-1569, effective October 1, 1989. To avoid confusion, these sections will be referred to by their previous designations which were applicable on the date of the district court's final order. All other provisions of Virginia's Motor Vehicle Franchise laws will be referred to by their new designations.

1. **Background.** Respondent Saturn Distribution Corporation ("Saturn") was created in 1985 to design, manufacture and market a new automobile. Pet. App. 3. The dealer agreement which Saturn wishes to impose upon its dealers in Virginia includes as a nonnegotiable item mandatory mediation and binding arbitration as the exclusive remedy for resolving disputes between Saturn and the dealer, the express provisions in the proposed agreement being:

> Saturn and Dealer acknowledge that, at the state and federal levels, various courts and agencies would, in the absence of this Article 5, be available to them to resolve claims or controversies which might arise between them. Saturn and Dealer agree that it is inconsistent with the Mission and Philosophy for either to use courts or governmental agencies to resolve such claims or controversies.
>
> THEREFORE, CONSISTENT WITH THE PROVISIONS OF THE UNITED STATES ARBITRATION ACT (9 U.S.C. Section 1 et seq.), DEALER AND SATURN AGREE THAT THE DISPUTE RESOLUTION PROCESS OUTLINED IN THIS ARTICLE, WHICH INCLUDES BINDING ARBITRATION, SHALL BE THE EXCLUSIVE MECHANISM FOR RESOLVING ANY CONTROVERSY OR CLAIM BETWEEN THEM ARISING OUT OF OR RELATING TO THIS AGREEMENT, ITS CREATION, OR TERMINATION.

Pet. App. 29-30 n.2.

Section 46.1-550.5:24 requires that such a dealer agreement be "approved by the Commissioner as not containing terms inconsistent with the provisions of this chapter" before it is offered to prospective dealers in Virginia. Pet. App. 49. Section 46.1-550.5:27(10) provides that it is unlawful to fail to include in such a dealer agreement the following language, "or words to that effect":

> "If any provision herein contravenes the valid laws or regulations of any state or other jurisdiction wherein this agreement is to be performed, or denies access to the procedures, forums, or remedies provided for by such laws or regulations,

> such provision shall be deemed to be modified to conform to such laws or regulations, and all other terms and provisions shall remain in full force and effect,". . . . [2]

Pet. App. 50.

When Saturn submitted its proposed agreement to the Commissioner for approval pursuant to § 46.1-550.5:24 (Joint Appendix in the Circuit Court ("J.A.") at 58-9), the Commissioner replied that "DMV cannot approve the Saturn Distribution Corporation Dealer Agreement" because, in part, "THE DISPUTE RESOLUTION PROCESS contravenes the Virginia franchise laws inasmuch as it requires that potential franchisees . . . give up access to the procedures, forums or remedies provided by such laws." J.A. at 83. However, the Commissioner emphasized that:

> I would have no problem approving [Saturn's] agreement if in the agreement, or in an addendum thereto, an option for the dealer to choose binding arbitration under Saturn's Dispute Resolution Process or to choose the forum provided under Virginia's dealer franchise laws is offered.
>
> It would then be clearly understood that those dealers choosing Saturn's Dispute Resolution Process would not be subject to protection under the Virginia franchise laws.

J.A. at 84.

Prior to Saturn's submission of its proposed agreement, Chrysler Motors Corp. and Freightliner (a truck manufacturing company) sent similar form agreements containing mandatory binding arbitration provisions to the Commissioner for approval pursuant to § 46.1-550.5:24. J.A. at 114. In both of these two previous cases, the Commissioner took the same position that he has maintained with Saturn. While he allowed the manufacturer/distributor to include a binding arbitration

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[2] Va. Code § 46.2-1569(9), the recodification of Va. Code § 46.1-550.5:27(10), contains identical language except that it omits "and effect" from the last phrase of the language required to be included in all franchises with motor vehicle dealers.

clause in the franchise agreement offered to Virginia dealers, the Commissioner required that the dealer be offered a choice between the use of binding arbitration or the "procedures, forums, and remedies provided for by" the laws of Virginia for dispute resolution. J.A. at 114-17.

2. **This Lawsuit.** On May 19, 1989, Saturn filed a complaint for declaratory judgment and injunctive relief against the Commissioner requesting the district court to declare (1) that §§ 46.1-550.5:24 and 46.1-550.5:27 are preempted by the FAA under the Supremacy Clause of the United States Constitution and (2) that the provisions of the Saturn dealer agreement mandating arbitration are valid and enforceable in Virginia. Pet. App. 32. Jurisdiction in the district court was based on 42 U.S.C. § 1331. *Id.* Virginia Automobile Dealers Association intervened as a co-defendant with the Commissioner and in opposition to Saturn. VADA is a trade association consisting of more than 600 franchised automobile dealers in Virginia. *Id.* On August 17, 1989, the district court entered a final order granting summary judgment in favor of Commissioner and VADA. Pet. App. 41.

3. **The District Court's Opinion.** Applying this Court's preemption analysis, the district court concluded that the Virginia statute, as interpreted by the Commissioner, "in no way 'stands as an obstacle to the accomplishment and execution of the full purposes and objectives' of the Federal Arbitration Act." Pet. App. 36 (quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941)). Noting that various Virginia statutes dictate the form of certain contracts with no opportunity for negotiation, the court concluded that § 46.1-550.5:27, in contrast, does not single out arbitration clauses for special treatment that burden parties' ability to commit themselves to arbitration. Pet. App. 34-35. Moreover, citing this Court's decision in *Volt Information Sciences, Inc. v. Board of Trustees*, 109 S. Ct. 1248, 1254 (1989) ("Arbitration under the Act is a matter of consent, not coercion."), the district court found that the challenged statute furthered the accomplishment of the full objectives of the FAA because it ensured consensual rather than forced arbitration. Pet. App. 36.

The district court distinguished several cases which Saturn cited in support of its motion. The court noted that *Collins Radio Co. v. Ex-Cell-O Corp.*, 467 F.2d 995 (8th Cir. 1972) and *Webb v. R. Rowland & Co., Inc.*, 800 F.2d 803 (8th Cir. 1986) both involved existing agreements to arbitrate and state statutes which explicitly singled out arbitration agreements. Pet. App. 37. The district court also had before it the lower court's opinion in *Securities Industry Ass'n v. Connolly*, 703 F. Supp. 146 (D. Mass. 1988), later affirmed by the First Circuit. The district court observed that the defendants in *Connolly* admitted that their regulations singled out arbitration agreements. Pet. App. 38.

4. **The Court Of Appeals' Opinions.** a. The Panel Majority. A divided panel of the court of appeals reversed the district court and found that § 46.1-550.5:27, but not § 46.1-550.5:24, was preempted. Emphasizing the value of arbitration as a means of dispute resolution and the " 'liberal federal policy favoring arbitration agreements' " (Pet. App. 6 (quoting *Moses H. Cone Memorial Hospital v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983)), the panel majority concluded that "if a state law singles out arbitration agreements and limits their enforceability it is preempted." Pet. App. 7. They first found that the FAA applied to laws of contract formation because, to hold otherwise, "would be to allow states to 'wholly eviscerate Congressional intent to place arbitration agreements upon the same footing as other contracts.' " Pet. App. 8 (quoting *Southland Corp. v. Keating*, 465 U.S. 1, 16-17 n.11 (1984)). Adopting the Fourth Circuit's dicta in *Supak & Sons Mfg. Co., Inc. v. Pervel Industries, Inc.*, 593 F.2d 135 (4th Cir. 1979), they held "that § 2 [of the Act] does preempt state rules of contract formation which single out arbitration clauses and unreasonably burden the ability to form arbitration agreements." Pet. App. 9. Applying this analysis, the panel majority found that § 46.1-550.5:27 "conflicts with the FAA because Virginia law generally permits contracting parties to make terms nonnegotiable, and singles out arbitration provisions as an exception to that rule." Pet. App. 11.

To conclude that § 46.1-550.5:27 singles out arbitration agreements, the panel majority relied heavily on the First Circuit's decision in *Securities Industry Ass'n v. Connolly*, 883 F.2d 1114 (1st Cir. 1989), *cert. denied*, 110 S. Ct. 2559 (1990). They considered non-determinative the fact that Virginia's statute neither expressly mentions arbitration nor is confined in its scope to that one specific type of forum selection clause. Pet. App. 12-13. Rather, to decide whether § 46.1-550.5:27 is a rule specifically tailored toward arbitration agreements or whether it is merely a part of Virginia's laws of contract formation, the panel majority compared it to general common law and statutory law and concluded that the challenged statute is preempted because, as a general rule, Virginia does not bar parties from making certain provisions of their contracts nonnegotiable. Pet. App. 13-16.

b. The dissent. Judge H. Emory Widener, Jr., dissented from the panel's opinion. Explaining that the majority had abandoned the proper preemption analysis, he pointed out that the "appropriate starting point in examining the statute in question is not a 'liberal federal policy favoring arbitration agreements' " (Pet. App. 21), but rather is a presumption against preemption "absent a clear and manifest Congressional intent to the contrary." *Id.* Noting that by its terms, the FAA does not apply until an arbitration agreement exists and that "virtually every reported case" in which the FAA has been held to preempt state law has dealt with the enforceability of an otherwise valid arbitration agreement, Judge Widener pointed out that the challenged statute deals with the formation of arbitration agreements, not their enforceability. Pet. App. 22. He found that § 46.1-550.5:27 "only precludes Saturn from unilaterally imposing agreements to arbitrate upon its dealers. If a dealer agrees to arbitrate, the Virginia statute is no impediment to the agreement's enforceability." *Id.* He concluded that there is no direct conflict between Virginia's statute and the FAA and thus no preemption. *Id.*

Judge Widener also explained that the majority panel had failed to recognize that the Dealer's Day in Court Act (15 U.S.C. §§ 1221-1225), overrode the FAA's congressional

mandate to enforce arbitration agreements by providing automobile dealers access to federal courts irrespective of contractual provisions. Pet. App. 22-25. He observed that the Dealer's Day in Court Act is "relevant not only to whether an exception to preemption exists, but, especially under a 'frustrate the federal policy' theory, to whether preemption should apply in the first instance." Pet. App. 25.

As did the district court, Judge Widener distinguished the *Connolly* decision. He considered the First Circuit's underlying concern in *Connolly*, to alleviate crowded court dockets, impermissible under Article III of the Constitution. Pet. App. 26. He also pointed out that *Connolly* was a securities case, an area in which federal acts have granted concurrent power to the states and in which this Court has addressed the effect of the FAA. *Id.* By contrast, Judge Widener observed, "the Virginia statute arises not from a grant of concurrent power, but from the State's inherent police power, and Congress in the DDCA did manifest an intent to preclude waiver of a judicial forum for claims between automobile dealers and manufacturers." Pet. App. 27.

c. A petition for panel rehearing and a suggestion for rehearing in banc was denied. The court of appeals granted a stay pending the timely filing of a petition for writ of certiorari.

REASONS FOR GRANTING THE WRIT

This case presents important issues concerning the FAA and the preemption of state law. The state statute at issue in this case ensures that a Virginia automobile dealer's decision to waive access to available "procedures, forums, or remedies" by agreeing to Saturn's mandatory and binding arbitration is voluntary. The panel majority held that the preemptive effect of the FAA under the Supremacy Clause reached state laws concerning contract formation and that Virginia's statute was preempted because, they concluded, it singles out arbitration clauses and unreasonably burdens the ability to form arbitration agreements. The approach taken by the panel majority in striking this statute down is a serious

departure from the language, legislative history and this Court's interpretation of the FAA and demonstrates an excessive enthusiasm for arbitration rather than an objective application of this Court's preemption analysis. By reviewing this case, this Court will have the opportunity to consider a decision which, if left unchallenged, will not only severely weaken the ability of Virginia and her sister states to exercise traditional police powers in protecting automobile dealers from the overwhelming economic power and bargaining strength of manufacturers/distributors, but will also cripple the states' ability to ensure their citizens voluntary access to all dispute resolution processes. The questions raised by the Fourth Circuit's decision are of widespread significance and review by this Court is warranted.

I. The Panel Majority Erroneously Held That The Federal Arbitration Act Applies To State Laws Of Contract Formation.

The Fourth Circuit erred in holding that the Federal Arbitration Act applied to § 46.1-550.5:27, a state law of contract formation. The panel majority conclusion is contrary to the express language of the FAA and its legislative history, both of which clearly demonstrate that the Act applies only to the *enforcement* of existing, consensual arbitration agreements.

Interpretation of a statute must start with its language and the words chosen by Congress must be accorded their ordinary meaning. *United States v. James*, 478 U.S. 597, 604 (1986); *American Tobacco Co. v. Patterson*, 456 U.S. 63, 68 (1982). The provisions of the FAA limit its application to the *enforcement* of agreements to arbitrate. Section 2 of the FAA reads:

> *A written provision in any . . . contract* evidencing a transaction involving commerce *to settle by arbitration* a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, *or an agreement in writing to submit to arbitration* an existing controversy arising out of such a contract, transaction, or

> refusal, *shall be* valid, irrevocable, and *enforceable*, save upon such grounds as exist at law or in equity for the revocation of any contract.

Pet. App. 46 (emphasis added). By its plain language, the Act applies only to enforce an agreement to arbitrate. It does not apply to state laws of contract formation.

The language of the FAA must be considered conclusive in the absence of a "clearly expressed legislative intention to the contrary." *Consumer Product Safety Commission v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980). The FAA's legislative history does not justify departure from the plain language of the Act; rather, the legislative history supports the conclusion that the FAA applies only to enforce arbitration contracts. The intent of Congress in enacting the FAA was modest. The FAA was designed simply to overcome traditional judicial resistance to the enforcement of voluntary arbitration agreements between contracting parties. The official reports of the two bills, which ultimately were codified as the FAA (H.R. 646 and S. 1005), underscore the limited scope of the legislation. Congressman Graham, who authored the House Report of H.R. 646, summarized the effect of the bill for his colleagues as follows:

> Arbitration agreements are purely matters of contract, and the effect of the bill is simply to make the contracting party live up to his agreement. He can no longer refuse to perform his contract when it becomes disadvantageous to him.

H. R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924). *See also Southland Corp. v. Keating*, 465 U.S. 1, 25 (1984) (O'Connor, J., dissenting); *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 419 (1967) (Black, J., dissenting). Addressing the fears of Congress that the legislation would supplant state law, Mr. Julius Cohen, one of the chief draftsmen of the legislation, stated that the proposed act would not supersede state law on contract formation:

> [The FAA] is no infringement upon the right of each State to decide for itself what contracts shall or shall not exist under its laws. To be sure whether or not a contract exists is a question of the substantive

> law of the jurisdiction wherein the contract was made.

Joint Hearings on S. 1005 and H.R. 646 before the Subcommittees of the Committees of the Judiciary, 68th Cong., 1st Sess. 37 (1924). *See also* Cohen & Dayton, *The New Federal Arbitration Law*, 12 Va. L. Rev. 265 (1926). There is nothing in the record of the congressional hearings to even suggest that the Act would affect the states' power to regulate the process of contract formation.

This Court consistently has emphasized the intent of the FAA's draftsmen and "honor[ed] the plain meaning of the [Act]." *Prima Paint*, 388 U.S. at 404. Writing for a unanimous Court in *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213 (1985), Justice Marshall stated:

> The legislative history of the Act establishes that the purpose behind its passage was to ensure judicial enforcement of privately made agreements to arbitrate. We therefore reject the suggestion that the overriding goal of the Arbitration Act was to promote the expeditious resolution of claims. The Act, after all, does not mandate the arbitration of all claims, *but merely the enforcement* – upon the motion of one of the parties – of privately negotiated arbitration agreements.
>
> * * *
>
> [P]assage of the Act was motivated, first and foremost, by a congressional desire to enforce agreements into which parties had entered, and we must not overlook this principal objective when construing the statute, or allow the fortuitous impact of the Act on efficient dispute resolution to overshadow the underlying motivation.

Id. at 219-21 (footnote omitted) (emphasis added). *See also, Volt Information Sciences, Inc. v. Board of Trustees*, 109 S. Ct. 1248, 1255 (1989); *Prima Paint*, 388 U.S. at 412-13 (Black, J., dissenting) ("Sections 2 and 3 of the Act assume the existence of a valid contract. They merely provide for enforcement where such valid contract exists.").

The FAA's unambiguous provisions and legislative history limit its application to the enforcement of arbitration agreements. Thus, the Eighth Circuit has observed that "[w]hile federal law may govern the interpretation and enforcement of a valid arbitration agreement, state law governs the question of whether such an agreement exists in the first instance." *Eassa Properties v. Shearson Lehman Bros., Inc.*, 851 F.2d 1301, 1304-5 n.7 (11th Cir. 1988). Because § 46.1-550.5:27 is a law of contract formation which does not affect the enforceability of forum selection clauses in agreements voluntarily executed, the FAA does not apply.

Without discussing the language of the Act or its legislative history, the Fourth Circuit panel majority cites this Court's opinion in *Southland* as supporting precedent for expanding the scope of the FAA beyond its purpose and provisions to reach Virginia's statute.[3] However, "[t]he issue of 'the making of an arbitration agreement' was not involved in *Southland*." *Hull v. Norcom, Inc.*, 750 F.2d 1547, 1551 (11th Cir. 1985). The question presented in *Southland* was whether California could render arbitration provisions in existing franchise agreements unenforceable by enacting a franchise investment law which invalidated any portion of an agreement waiving compliance with state law. This Court held that:

> Plainly the effect of the judgment of the California court [in upholding the state statute] is to nullify a

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[3] However, as in *all* the FAA cases which this Court has decided, there was an existing agreement to arbitrate in *Southland*. *Id.* at 4. *See also Rodriguez De Quijas v. Shearson/American Express, Inc.*, 109 S. Ct. 1917, 1918-19 (1989); *Volt Information Sciences*, 109 S. Ct. at 1251; *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 223 (1987); *Perry v. Thomas*, 482 U.S. 483, 485 (1987); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 617 (1985); *Byrd*, 470 U.S. at 215; *Moses H. Cone Memorial Hospital v. Mercury Constr. Corp.*, 460 U.S. 1, 5 (1983); *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 508 (1974); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Ware*, 414 U.S. 117, 121-22 (1973); *Prima Paint*, 388 U.S. at 398; *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 199 (1956).

> valid contract made by private parties under which they agreed to submit all contract disputes to final, binding arbitration.

Id. at 7. The statute in *Southland* not only voided otherwise valid arbitration contracts, it mandated that franchise disputes be submitted to *judicial* resolution rather than any other dispute resolution forum. These facts formed the basis on which this Court concluded that the state law was preempted:

> The California Supreme Court interpreted *this statute to require judicial consideration of claims* brought under the state statute and accordingly refused to enforce the parties' contract to arbitrate such claims. *So interpreted* the California Franchise Investment Law directly conflicts with § 2 of the Federal Arbitration Act and violates the Supremacy Clause.
>
> In enacting § 2 of the federal Act, Congress declared a national policy favoring arbitration and withdrew the power of the states to require a *judicial forum* for the resolution of claims which the contracting parties agreed to resolve by arbitration.

Id. at 10 (emphasis added). Therefore, this Court's concern about a state's ability to "undercut the *enforceability* of arbitration agreements" (*Id.* at 16) (emphasis added) or "wholly eviscerate Congressional intent" (*Id.* at 16 n.11) pertained to state laws which would mandate judicial resolution of claims and prohibit the enforcement of agreements to arbitrate even though parties have previously agreed to submit their disputes to arbitration.[4] By contrast, § 46.1-550.5:27 is a law of contract formation which does not impinge upon the enforceability of agreements to adopt any form of dispute resolution. It does not mandate judicial resolution of disputes.[5]

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[4] Similarly, in *Perry v. Thomas* the state statute which this Court held as being preempted by the FAA required that litigants be provided a judicial forum for resolving wage disputes even though the employees had executed agreements with their employers containing arbitration provisions. *Id.* at 491.

[5] Section 46.1-550.5:27 must be read in conjunction with § 46.1-550.5:24 (upheld by the Fourth Circuit), which requires that each

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As pointed out in Judge Widener's dissent, the panel majority's conclusion that the FAA applies to state laws of contract formation such as § 46.1-550.5:27 rests on a single case: *Securities Industry Ass'n v. Connolly*, 883 F.2d 1114 (1st Cir. 1989), *cert. denied*, 110 S. Ct. 2559 (1990). This Court has consistently interpreted the Act's provisions as applying only to the enforcement of an arbitration agreement. No case cited by *Connolly* holds to the contrary.[6]

II. The Panel Majority's Preemption Analysis Was Erroneous In Holding That There Was An Actual Conflict Between The Federal Arbitration Act And § 46.1-550.5:27 Warranting Preemption.

Even if the FAA applied to state laws of contract formation, the Act would still not preempt § 46.1-550.5:27 because there is no actual conflict between the two statutes. This Court has held that the proper starting point for preemption analysis is "the presumption against finding pre-emption of state law in areas traditionally regulated by the States" absent a "clear and manifest purpose of Congress" to the contrary.

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automobile manufacturer/distributor seek and receive the approval of the Commissioner to offer a franchise agreement form to its dealers in Virginia before it actually does so. Automobile dealer franchises are one type of only a handful of contracts which must be reviewed and approved by state agencies before they are executed within the Commonwealth. *See, e.g., Va. Code* § 38.2-203. It would be virtually impossible for Virginia to enforce legislation requiring all or even most contracts offered in the Commonwealth to be reviewed and approved by a state agency *before* they are executed. Therefore, Virginia uses this procedure sparingly and only when critical state interests exist, such as the protection of automobile dealers, as explained in Section V of this petition.

[6] In all the cases which this Court has decided concerning the FAA, the disputes concerned the enforcement of existing agreements to arbitrate. *See* Pet. at 12 n.3. This Court has yet to consider specifically whether the FAA preempts state statutes concerning contract formation in the absence of an executed arbitration contract. This case would provide this Court with an opportunity to resolve this question.

California v. ARC America Corp., 109 S. Ct. 1661, 1665 (1989). *See also Bethlehem Steel Co. v. New York State Labor Relations Board*, 330 U.S. 767, 780 (1947) (Frankfurter, J., dissenting). Solicitor General Kenneth W. Starr, in his unpublished monograph "The Law of Preemption," observed that " 'our federal system, with its high regard for the several States' powers of governance, requires that judges not pre-empt state laws lightly.' " *Dewey v. R.J. Reynolds Tobacco Co.*, 1990 N.J. LEXIS 98, 48 (N.J. 1990) (quoting Starr, "The Law of Preemption," at 61).

This Court recently reiterated its preemption analysis in *English v. General Electric Co.*, 110 S. Ct. 2270 (1990):

> Our cases have established that state law is pre-empted under the Supremacy Clause in three circumstances. First, Congress can define explicitly the extent to which its enactments pre-empt state law . . . . Second, in the absence of explicit statutory language, state law is pre-empted where it regulates conduct in a field that Congress intended the Federal Government to occupy exclusively . . . . Finally, state law is pre-empted to the extent that it actually conflicts with federal law.

Id. at 2275 (citation omitted).[7] Justice Blackmun, writing for a unanimous court, stressed the difficult burden a party bears in arguing that a state law is preempted by a federal law:

> "Undoubtedly, every subject that merits congressional legislation is, by definition, a subject of national concern. That cannot mean, however, that every federal statute ousts all related state law. . . . Instead, we must look for special features warranting pre-emption."

Id. at 2279 (quoting *Hillsborough County v. Automated Medical Laboratories, Inc.*, 471 U.S. 707, 719 (1985)). Justice Blackmun also stated that:

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[7] In *Volt Information Sciences*, this Court limited the preemption analysis of the FAA to the third circumstance, where a state law "actually conflicts" with the Act: "The FAA contains no express pre-emption provision, nor does it reflect a congressional intent to occupy the entire field of arbitration." *Id.* at 1254.

> The Court has observed repeatedly that pre-emption is ordinarily not to be implied absent an "actual conflict." The "teaching of this Court's decisions . . . enjoins seeking out conflicts between state and federal regulation where none clearly exists."

Id. at 2281 (citation omitted) (quoting *Huron Portland Cement Co. v. Detroit*, 362 U.S. 440, 446 (1960)).

Under this Court's preemption analysis, there is no actual conflict between § 46.1-550.5:27 and the FAA. The Virginia statute, as interpreted by the Commissioner, disturbs neither the parties' ability to agree to arbitrate their disputes, nor the right to enforce such an agreement.[8] Instead, it simply requires that both parties consent to a dispute resolution forum, such as arbitration – that arbitration be "a matter of consent, not coercion." *Volt Information Sciences*, 109 S. Ct. at 1255. The FAA does not preempt § 46.1-550.5:27, which furthers rather than frustrates the intent of the FAA by ensuring that arbitration is truly consensual.

In reaching the opposite conclusion, the panel majority unduly emphasized the " 'liberal federal policy favoring arbitration agreements.' " Pet. App. 6 (quoting *Moses H. Cone Memorial Hospital*, 460 U.S. at 24). They failed to recognize that the federal policy favoring arbitration does not avoid the necessity to apply this Court's accepted preemption analysis to test the validity of the challenged statutes.[9] More

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[8] Because the Commissioner is responsible for administering and enforcing the statutory provisions, his interpretation must be considered in discerning their meaning. *Hoffman Estates v. Flipside, Hoffman Estates, Inc.*, 455 U.S. 489, 494 n.5 (1982).

[9] This Court on occasion has been less than diligent in recognizing and fully discussing the accepted preemption analysis where there is tension between federal and state legislation in cases involving arbitration. For example, in *Southland* amazingly there is no mention of preemption in the majority opinion; it is only discussed by Justice Stevens in his dissent. *Id.* at 18. In *Perry*, although preemption is alluded to in the majority opinion, there is no analysis; in Justice Stevens' and Justice O'Connor's dissents it is discussed. *Id.* at 493-95. But in *Ware*, the

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importantly, the panel majority failed to consider this Court's teaching in *Hillsborough County*, 471 U.S 707 at 719, for, as Judge Widener pointed out in his dissent, not only the FAA, but "[e]very federal statute presumably was enacted to further a strong or liberal federal policy in favor of or against something, but that does not lead inexorably to preemption of every state law that touches on the same subject matter." Pet. App. 21.

III. The Panel Majority Erroneously Concluded That The Virginia Statute Singled Out Arbitration Provisions For Special Treatment And Placed An Unreasonable Burden On Parties' Ability To Enter Into Arbitration Agreements.

As discussed above, it is evident that there is no "actual conflict" between the FAA and the challenged statute and thus no preemption. That should end the inquiry. However, the panel majority held that "§ 2 [of the Act] preempt[s] state rules of contract formation which single out arbitration clauses and unreasonably burden the ability to form arbitration agreements." Pet. App. 9. The panel majority erred because § 46.1-550.5:27 neither singles out arbitration clauses nor unreasonably burdens the parties' ability to enter into arbitration agreements.

This Court has recognized that "the purpose of Congress in 1925 [in enacting the FAA] was to make arbitration agreements as enforceable as other contracts, *but not more so*." *Prima Paint*, 388 U.S. at 404 n.12 (emphasis added). Virginia's statute does exactly that. As part of the protective

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preemption analysis is set out clearly, recognizing the difference between conflicting federal regulatory schemes (as in *Scherk*, *Byrd*, *McMahon* and *Rodriguez*) and the interrelationship between federal and state statutes such as presented in the present case. *Ware*, 414 U.S. at 126-27. Most recently, this Court in unmistakable terms rejected FAA preemption of the California choice of law statute in *Volt Information Sciences* applying the traditional analysis. *Id.* at 1254-55.

scheme for automobile dealers, § 46.1-550.5:27 does not address arbitration specifically. Indeed, arbitration is not mentioned because it is not the only type of forum selection clause nor the only method of dispute resolution.[10] The challenged statute applies to any forum selection clause having the effect of denying dealers access to "procedures, forums, or remedies" provided by law where the contract is to be performed. For example, if Saturn proposed a form agreement which required that all grievances by its Virginia dealers be resolved in Michigan courts (not by arbitration), the Commissioner would not permit that provision to be forced upon dealers, because it would deny the dealers access to the procedures, forums or remedies provided under Virginia's automobile dealer laws. Likewise, any mandatory and binding mediation provision in a manufacturer/distributor franchise form offered on a nonnegotiable basis would be contrary to Virginia laws. Thus the challenged statute does *not* "take its meaning precisely from the fact that a contract to arbitrate is at issue." *Perry*, 482 U.S. at 492 n.9. Section 46.1-550.5:27 does not single out arbitration agreements for special treatment, but instead treats them the same as other forum selection provisions which are otherwise valid in Virginia.

The panel majority cites *Southland* and *Perry* as supporting their finding that even if a statute affects all forum selection and does not expressly refer to arbitration, it still may impermissably single out arbitration provisions. Pet. App. 12-13. However, *Southland* and *Perry* are not apposite; this Court did not hold that the California statutes violated the FAA because they singled out arbitration. Rather, this Court

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[10] Dispute resolution forums include, at least: judicial, early neutral evaluation and case management, mediation, court supervised criticism, neighborhood justice centers, counseling, mini-trials, fact finding, malpractice screening panels, statutory administrative procedures, court annexed arbitration and arbitration. *See, generally*, Lieberman and Henry, *Lessons from the Alternative Dispute Resolution Movement*, 53 U. Chi. L. Rev. 424 (1986); Patterson, *Dispute Resolution in a World of Alternatives*, 37 Cath. U. L. Rev. 591, 592 (1988) ("The number of possible processes for resolving disputes is virtually infinite.").

found that the state statutes in both cases ran afoul of the Act because they voided existing arbitration contracts by requiring judicial resolution of claims. *Southland*, 465 U.S. at 10; *Perry*, 482 U.S. at 490-91.

The panel majority maintained that the challenged statute "must be compared to *general* contract law rather than to laws which apply only to contracts subject to the Motor Vehicle Licensing Act." Pet. App. 13-14 (original emphasis). In reaching that conclusion, the panel majority relied heavily on one decision, *Connolly*. However, *Connolly* is readily distinguishable on its facts. In *Connolly*, the Commonwealth of Massachusetts admitted that its regulations applied *only* to arbitration agreements. *Id.* at 1120. In the present case, by contrast, § 46.1-550.5:27 does not single out arbitration but treats it on an equal footing with other contract provisions that are otherwise valid.

In addition, the legal analysis in *Connolly* is flawed. The First Circuit concluded, and the panel majority in the present case agreed, that a state law of contract formation which treats arbitration agreements in a specific industry "more severely than . . . contracts are generally treated under" state law is invalid. *Id.* at 1124. Thus, adopting the analysis in *Connolly*, the panel majority held that the correct comparison group for the challenged statute was "*general* contract law" or, in other words, the entire spectrum of contracts.

When *Connolly* was on appeal before this Court, however, the Solicitor General advocated a smaller comparison group. In his Brief for the United States as Amicus Curiae (the "Solicitor General's Brief"), the Solicitor General repeatedly emphasized that Massachusetts had conceded that its regulations singled out arbitration. Solicitor General's Brief at 7, 8, 11 and 15. Based on this concession, he concluded that further review of *Connolly* was unwarranted. *Id.* at 11. However, drawing a distinction between statutes which single out arbitration and "permissible state regulations of general application that necessarily encompass arbitration provisions in contracts" (*Id.* at 11), the Solicitor General counseled that Massachusetts was not powerless in its ability to regulate arbitration:

> Absent controlling federal law, the state legislature presumably *could accomplish the goal of the securities arbitration regulations* by enacting a state law providing, for example, that *forum selection clauses* in all *consumer contracts* must be the subject of negotiation and full disclosure. In other words, application of the anti-discrimination principle of Section 2 of the Federal Arbitration Act is by no means tantamount to outlawing state regulation of arbitration provisions. Federal law simply guarantees that arbitration agreements not be singled out for special treatment. That is precisely what Massachusetts attempted to do here.

Id. at 19-20 (emphasis added) (citation omitted).[11] It is obvious from his brief that the Solicitor General does not take the position that a state law exercising its legitimate police power must apply to *all contracts* in order to avoid falling prey to an accusation that it singles out arbitration agreements. Crucial to his example of a permissible statute is the legislation's application to other provisions – i.e. "forum selection clauses" – rather than exclusively to arbitration provisions as Massachusetts had done. Thus, the Solicitor General concluded that a statute need not apply to the total sphere of contracts, but rather to only "consumer contracts." A requirement that state statutes do otherwise – that they apply to *all* contracts – would cripple the states' ability to address evenhandedly arbitration clauses in concert with other forum selection clauses in a more limited group of contracts.[12]

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[11] In his brief, the Solicitor General did not specifically address the question of whether the FAA applies to laws of contract formation.

[12] The panel majority's opinion, if left standing, would transform arbitration into a "sacred cow." As discussed in Section I of this petition, the language and the legislative history of the Act confine its scope to the enforcement of existing arbitration agreements. *See* Pet. at 9-14. In this context, the "savings clause" of the FAA – that an arbitration agreement is enforceable "save upon such grounds as exist at law or in equity for the

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Because the challenged Virginia statute applies to all provisions by which a dealer could waive access to any available "procedures, forums, or remedies," it does not "single out arbitration." As Judge Widener said in his dissent, "As interpreted by the Commissioner, the statute only precludes Saturn from unilaterally imposing agreements to arbitrate upon its dealers. If a dealer agrees to arbitrate, the Virginia statute is no impediment to the agreement's enforceability." Pet. App. 22.

IV. The Panel Majority Failed To Find That The Federal Arbitration Act Would Conflict With The "Dealer's Day In Court Act" If Virginia Dealers Were Forced To Accept Mandatory Arbitration.

An interpretation that the FAA authorizes manufacturers/distributors to force an arbitration agreement on motor vehicle dealers would conflict with the Dealer's Day in Court Act ("DDCA"), 15 U.S.C. §§ 1221-1225. The Dealer's Day in Court Act demonstrates that Congress intended dealers to have access to courts to seek redress against distributors.

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revocation of any contract" – is consistent with Congress' purpose in passing the legislation, which was to make existing arbitration agreements as enforceable as other contracts, but not more so. *See Prima Paint*, 388 U.S. at 404 n.12; Pet. at 17. The panel majority, however, after re-tooling the Act to make it apply to state laws of contract formation, then plugs in the "savings clause," resulting in the sweeping preemption of any state statute which "imposes burdens on arbitration agreements that do not apply to contracts generally." Pet. App. 13. Therefore, if this decision goes unchallenged, any state law applying to the formation of specific agreements by regulating the use of certain types of contract provisions which are otherwise valid, but which necessarily encompass arbitration, would be preempted by the FAA because the law does not apply to contracts generally. As a result, the panel majority's interpretation of the FAA does more than place arbitration agreements on equal footing with other contract provisions; it elevates arbitration to the status of an untouchable. The ramifications of this interpretation on the exercise of the states' traditional police powers are far-reaching.

The FAA's "mandate may be overrridden by a contrary congressional command." *McMahon*, 482 U.S. at 226. *See also Mitsubishi*, 473 U.S. at 627-28. Congressional intent to prohibit waiver of a judicial remedy for a statutory right can be deduced from a statute's text or legislative history, "or from an inherent conflict between arbitration and the statute's underlying purposes." *McMahon*, 482 U.S. at 227. Enacted over three decades after the original Federal Arbitration Act, the DDCA provides that:

> An automobile dealer may bring suit against any automobile manufacturer . . . in any district court of the United States . . . [to] recover damages by him sustained . . . by reason of the failure of . . . [the] manufacturer . . . to act in good faith in performing or complying with any of the terms or provisions of the franchise, or in terminating, canceling, or not renewing the franchise with said dealer. . . .

15 U.S.C. § 1222. The text of the DDCA is consistent with the underlying purpose behind it, as indicated in the legislative history:

> The bill *creates a cause of action* where none previously existed in that, *irrespective of contractual provisions, it grants a right of review in the Federal courts* of disputes between automobile manufacturers and their dealers involving the good faith of the manufacturer in complying with, in terminating, or in not renewing the franchises.

H.R. Rep. No. 2850, 84th Cong., 2d Sess., *reprinted in* 3 U.S. Code Cong. & Ad. News 4596, 4596 (1956) (emphasis added). Therefore, the provisions of the DDCA and its legislative history manifest a Congressional intent to prohibit a mandatory waiver of a judicial forum by automobile dealers. *See Barney Motor Sales v. Cal Sales, Inc.*, 178 F. Supp. 172, 174 (S.D. Cal. 1959).

There would be an inherent conflict between the FAA and the more recently enacted DDCA if automobile dealers in Virginia (and throughout the country) could be forced to accept arbitration because Congress' attempt to balance the disparity in the bargaining position between manufacturers/

distributors and dealers would be frustrated. Congress would not have enacted the DDCA if the right of access it granted to dealers could be taken away by the unilateral action of manufacturers/distributors, the very ones from whom Congress sought to protect the dealers. However, it would be entirely consistent with the FAA, the DDCA and the challenged Virginia statute if a dealer could *voluntarily* waive his rights under these dealer protective statutes and agree to arbitrate all disputes which may arise out of a franchise agreement. *See Schmitt-Norton Ford, Inc. v. Ford Motor Co.*, 524 F. Supp. 1099, 1105 (D. Minn. 1981), *aff'd*, 685 F.2d 438 (8th Cir. 1982). This accommodation among the various statutes may be achieved under the Commissioner's interpretation of the challenged statute.

Declining to decide "whether all DDCA claims may be arbitrated," the panel majority stated that "[e]ven if the DDCA does preclude waiver of a judicial forum for the enforcement of its rights, the Virginia statutes do not mirror that restriction but also preclude some waivers of a judicial forum for the enforcement of non-DDCA claims." Pet. App. 7 n.2. As Judge Widener states in his dissent, the panel majority "both mischaracterizes the Virginia statute and understates the significance of the DDCA's legislative history." Pet. App. 23. Section 46.1-550.5:27 merely ensures that a dealer voluntarily waives his right to access to certain dispute resolution forums. It does not preclude the waiver of judicial forum for either DDCA or non-DDCA claims. In addition, the legislative history of the DDCA underscores the importance of granting dealers access to a judicial forum:

> Concentration of economic power in the automobile manufacturing industry of the United States has developed to the point where legislation is required to remedy the manifest disparity in the ability of franchised dealers of automobile vehicles to bargain with their manufacturers. . . . *The bill as amended proceeds from the conclusion that in the automobile industry concentration of economic power has increased to the degree that traditional contractual concepts are no longer adequate to protect the automobile dealers under their franchises.*

H.R. Rep. No. 2850, 84th Cong., 2d Sess., *reprinted in* 3 U.S. Code Cong. & Ad. News 4596, 4596-97 (1956) (emphasis added).

By enacting the Dealer's Day in Court Act, Congress acknowledged that an automobile dealer is in a uniquely vulnerable position in relation to his manufacturer/distributor and, as a result, it afforded the dealer a protection not shared by other franchisees. However, by ensuring a dealer's day in court against his manufacturer/distributor, Congress did not preempt the entire field of automobile franchise law.[13] Virginia's automobile franchise laws, of which the challenged statutes play an integral part, were enacted to advance the same interests which Congress recognized in passing the DDCA. As Judge Widener stated, "[I]f the most that can be said, as here, is that a presumptively valid state statute is in general tension with a federal statute of general application, and yet furthers precisely the same goals as another federal statute dealing with the specific subject in issue, the state enactment should stand until Congress says otherwise." Pet. App. 25. As a result, "the fact that the DDCA may not encompass every conceivable claim between manufacturer and dealer is of no consequence." Pet. App. 24-25 (Widener, J., dissenting).

V. The Panel Majority Failed To Uphold Virginia's Judicially Recognized Interest In Enforcing Its Automobile Franchise Laws To Promote Fair Dealing Between Manufacturers/Distributors And Their Dealers.

Virginia has enacted its motor vehicle franchise laws to prevent unfair acts or practices between a manufacturer/

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[13] 15 U.S.C. § 1225 expressly provides that the Act does "not invalidate any provision of the laws of any State except insofar as there is a direct conflict between an express provision of this [Act] and an express provision of State law which can not be reconciled." *See, e.g., American Motors Sales Corp. v. Division of Motor Vehicles*, 592 F.2d 219, 224 (4th Cir. 1979), *cert. denied*, 444 U.S. 836 (1979) (in upholding a portion of one of the statutes here under review, *Va. Code* § 46.1-550.5:27, the Fourth Circuit held that the Dealer's Day in Court Act did not preempt Virginia's ability to enact such laws).

distributor and its dealer. These laws recognize the vast disparity in bargaining power between the manufacturer/distributor and its dealer. By initiating this lawsuit, Saturn, a manufacturer/distributor, has attempted unilaterally to substitute its own arbitration process for the administrative and judicial procedures provided by Virginia law.

Motor vehicle franchise laws uniformly have been recognized as promoting legitimate state purposes. In *New Motor Vehicle Bd. v. Orrin W. Fox Co.*, 439 U.S. 96 (1978), this Court, interpreting California's automobile franchise laws, discussed the disparity in bargaining power between automobile manufacturers and their dealers:

> "[The] vast disparity in economic power and bargaining strength [between manufacturers and the dealers] has enabled the factory to determine arbitrarily the rules by which the two parties conduct their business affairs. These rules are incorporated in the sales agreement or franchise which the manufacturer has prepared for the dealer's signature.
>
> "Dealers are with few exceptions completely dependent on the manufacturer for their supply of cars. When the dealer has invested to the extent required to secure a franchise, he becomes in a real sense the economic captive of his manufacturer. The substantial investment of his own personal funds by the dealer in the business, the inability to convert easily the facilities to other uses, the dependence upon a single manufacturer for supply of automobiles, and the difficulty of obtaining a franchise from another manufacturer all contribute toward making the dealer an easy prey for domination by the factory. On the other hand, from the standpoint of the automobile manufacturer, any single dealer is expendable. The faults of the factory-dealer system are directly attributable to the superior market position of the manufacturer."

Id. at 100 n.4 (quoting S. Rep. No. 2073, 84th Cong., 2d Sess. 2 (1956)). This Court also noted that some states, including Virginia, had enacted legislation to protect car dealers. *Id.* at 101 n.5. After recognizing the authority of a state to enact a

"general scheme of business regulation that impose[s] reasonable restrictions upon the exercise of the right [to franchise]" (*Id.* at 106), this Court upheld California's Automobile Franchise Act. *Id.* at 108.[14]

At the heart of Virginia's motor vehicle dealer franchise laws is § 46.1-550.5:27 which provides, in connection with *Va. Code* § 46.2-1573, that the Commissioner may conduct hearings to determine, among other issues, whether: (1) the refusal of a manufacturer to permit a dealer to sell a franchise is reasonable under the circumstances; (2) there is reasonable evidence that after the grant of a new franchise in an existing dealer's market area, the market will support all of the dealers in the market area; (3) there is good cause to determine, cancel or refuse to renew the franchise of a dealer; or (4) the refusal to offer a dealer's designation of a successor is unreasonable under the circumstances. The Commissioner's decisions concerning disputes under Virginia's dealer franchise laws are binding on all interested parties, subject to appeal and judicial review. *Va. Code* § 46.2-1573.A. In sum, Virginia's dealer franchise laws provide substantive rules in a regulatory scheme to be administered by the Commissioner.

Mandatory application of Saturn's franchise agreement form with its binding arbitration would allow General Motors' subsidiary to unilaterally void Virginia's dealer protections. Saturn would reap the benefits of a Virginia market while being exempt from oversight by a neutral official, the Commissioner. The need for such oversight is clearly recognized by Congress and this Court. Virginia's General Assembly has created, by statute, specific procedural and

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[14] To suggest, as did the panel majority, "that no automobile dealer is required to contract with [Saturn]" and that "[d]ealers are not required to execute the new agreement in order to continue as dealers" (Pet. App. 16 n.6) is to ignore the economic captivity described by this Court. The reality is that the panel majority not only has put at risk all potential new dealers but all existing dealers upon renewal of their contracts. Chrysler Motor Corporation and Freightliner (and all other manufacturers/distributors) understandably will expect the Commissioner to approve their mandatory binding arbitration provisions as well. J.A. at 114-17.

substantive rights for dealer protection. This Court should not allow Saturn to demand those dealers to waive access to such procedures as a condition of being accepted as a franchisee.[15]

Reduced to its essence, Saturn's challenge is but another attempt by a national manufacturer/distributor to undermine Virginia's dealer protection statutes. In *American Motors*, the attack came under the guise of a Commerce Clause challenge. Saturn, a subsidiary of General Motors, now seeks to invalidate the dealer laws by means of the FAA and the Supremacy Clause. However, unlike the earlier attempt by American Motors, Saturn's challenge, if successful, would render Virginia's dealer protection statutes a nullity by permitting manufacturers to force dealers to waive all rights under the Virginia law.[16] As a result, Virginia's legitimate interest in enforcing its franchise laws would be frustrated.

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[15] Citing this Court's opinion in *Rodriguez De Quijas*, the panel majority noted that "[e]xisting Virginia law can and should be applied to revoke *any* contract which results from . . . the sort of *overwhelming* economic power which can render an agreement unconscionable." Pet. App. 19 (original emphasis). Having made that holding, the panel majority failed to take the next logical step in this analysis and acknowledge the overwhelming economic power wielded by automobile manufacturers/distributors which Congress and this Court have found to exist. As a result of the panel majority's opinion, there is no doubt that Saturn, or any other manufacturer/distributor, could impose its own arbitration scheme on its potential dealer or existing dealer (upon renewal) as a result of this overwhelming economic power, which would render such franchises unconscionable in the absence of statutes such as § 46.1-550.5:27. Only where a dealer has the option to choose is this avoided.

[16] This is not idle speculation. If the Virginia statute is preempted there would be nothing to protect dealers from being coerced into an arbitration agreement which provides that all disputes will be settled by arbitration in Michigan or Japan and under the laws of another state or country. This is precisely the kind of arbitration agreement that was at issue in *Mitsubishi*. The lower courts held that Puerto Rico could not *forbid enforcement* of such an arbitration agreement (although this Court did not address that issue) but they did *not* hold that a state could not act to protect the dealer (and the viability of its own statute) by requiring such an agreement to be voluntary.

CONCLUSION

The present case presents to this Court important issues, the resolution of which will impact on the traditional police powers of states and the doctrine of federalism. Squarely before this Court is the question of whether the preemptive effect of the FAA under the Supremacy Clause reaches state statutes concerning contract formation. If left undisturbed, the panel majority's conclusion that the Act does have such an expansive scope would infringe upon the states' ability to treat arbitration the same as all other contract provisions in the exercise of their traditional regulatory powers. Moreover, this Court now has its first opportunity to consider the Dealer's Day in Court Act, the states' dealer protection statutes and congressional and judicial findings concerning the overwhelming economic power wielded by automobile manufacturers/distributors, in the context of the FAA. Weighing in the balance is Virginia's and her sister states' ability not only to protect their automobile dealers, but also to ensure all their citizens voluntary access to all dispute resolution processes.

The petition for writ of certiorari should be granted.

Respectfully submitted,

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Commonwealth of Virginia
and
Virginia Automobile
Dealers Association, Inc.

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Appendix A

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 89-2773

SATURN DISTRIBUTION CORPORATION, a Delaware Corporation,

Plaintiff-Appellant,

versus

DONALD E. WILLIAMS, Commissioner of the Department of Motor Vehicles, Commonwealth of Virginia; VIRGINIA AUTOMOBILE DEALERS ASSOCIATION,

Defendants-Appellees,

CENTER FOR PUBLIC RESOURCES, INC.,

Amicus Curiae.

Appeal from the United States District Court for the Eastern District of Virginia, at Richmond. Richard L. Williams, District Judge. (CA-89-319-R)

Argued: December 6, 1989 Decided: June 6, 1990

Before WIDENER, CHAPMAN, and WILKINSON, Circuit Judges.

Reversed by published opinion. Judge Chapman wrote the opinion, in which Judge Wilkinson joined. Judge Widener wrote a dissenting opinion.

ARGUED: Kenneth Steven Geller, MAYER, BROWN, & PLATT, Washington, D.C., for Appellant. Guy Winston Horsley, Jr., Senior Assistant Attorney General, Richmond, Virginia; Robert Harvey Chappell, Jr., CHRISTIAN, BARTON, EPPS, BRENT & CHAPPELL, Richmond, Virginia, for Appellees. **ON BRIEF:** Richard J. Favretto, Evan M. Tager, MAYER, BROWN & PLATT, Washington, D.C.; Stephen M. Shapiro, MAYER, BROWN & PLATT, Chicago, Illinois; E. Milton Farley, III, David F. Peters, HUNTON & WILLIAMS, Richmond, Virginia; Roderick D. Gillum, Vice President and General Counsel, SATURN CORPORATION, Troy, Michigan, for Appellant. Mary Sue Terry, Attorney General, Walter A. McFarlane, Deputy Attorney General, Jeffrey A. Spencer, Assistant Attorney General, Eric K. G. Fiske, Assistant Attorney General, Richmond, Virginia; E. Ford Stephens, CHRISTIAN, BARTON, EPPS, BRENT & CHAPPELL, Richmond, Virginia; William T. Lehner, Malvin W. Brubaker, Richmond, Virginia, for Appellees. John A.C. Keith, BLANKENSHIP & KEITH, Fairfax, Virginia, for Amicus Curiae.

CHAPMAN, Circuit Judge:

Plaintiff/appellant Saturn Distribution Corporation appeals the denial of its motion for summary judgment and the grant of summary judgment against it by the district court. Saturn brought this action for declaratory

and injunctive relief against the Commissioner of the Virginia Department of Motor Vehicles to challenge two provisions of the Virginia Motor Vehicle Dealer Licensing Act. The central question raised below and on appeal is whether Virginia may prohibit the formation of a non-negotiable agreement between an automobile dealership and an automobile manufacturer compelling arbitration of claims arising out of the dealership agreement. The district court held that Virginia may enforce its statutory provisions designed to prevent the formation of mandatory arbitration agreements between automobile manufacturers and dealers. We hold that one of the challenged provisions is preempted by the Federal Arbitration Act, and therefore reverse.

I.

Saturn Distribution Corporation (Saturn) is a wholly-owned subsidiary of Saturn Corporation, which is in turn a wholly-owned subsidiary of General Motors Corporation. Saturn was created in 1985 to design, manufacture, and market motor vehicles under the "Saturn" nameplate. Saturn adopted a "Mission and Philosophy" of manufacturing and marketing cars, which is reflected in the *Saturn Distribution Corporation Dealer Agreement* (hereinafter "Dealer Agreement"). As part of that philosophy, Saturn concluded that an alternative dispute resolution system should be a core element of its Dealer Agreement. That system includes binding arbitration which is mandatory under the Agreement.[1]

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[1] If a dispute arises, either Saturn or a dealer may file a request for mediation. The dispute is forwarded to a panel,

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The Commonwealth of Virginia has enacted legislation that prohibits automobile manufacturers and dealers from entering into agreements that contain mandatory alternative dispute resolution provisions, such as Saturn's. Va. Code Ann. § 46.1-550.5:27 (1989 Supp.). In addition, a second statute requires a manufacturer to submit its standard franchise agreement to the Commissioner of the Department of Motor Vehicles for his approval prior to offering it to a dealer. Va. Code Ann. § 46.1-550.5:24 (1988 Supp.). When Saturn submitted its Dealer Agreement to the Commissioner, Donald E. Williams, he refused to approve it. The Commissioner subsequently made clear that he would not approve the Agreement unless it contained an opt out provision to the binding arbitration provisions. Saturn brought this action against the Commissioner alleging that the statutes, as applied by the Commissioner to its Dealership Agreement, are preempted by the Federal Arbitration Act. The Virginia Automobile Dealers Association (VADA) intervened as a defendant.

(Continued from previous page)

which recommends a consensus solution. If either party rejects that solution, or if both waive mediation, they proceed to binding arbitration, which provides for document discovery and a hearing. The Arbitration Panel, composed of two dealers and two Saturn representatives, is required to reach a consensus decision, which is final and unappealable, except as provided by the Federal Arbitration Act.

Since arbitration is central to the structure of its Dealership Agreement, Saturn refuses to contract with any dealer who will not agree to this mandatory arbitration clause. For this reason, this opinion refers to the arbitration clause as "nonnegotiable."

The district court ruled that the provisions are not preempted by the Federal Arbitration Act (FAA), 9 U.S.C. §§ 1 *et seq.*, and granted summary judgment to defendants. *Saturn Distrib. Corp. v. Williams*, 717 F. Supp. 1147 (E.D. Va. 1989). On appeal, the Center for Public Resources, Inc. submitted an amicus curiae brief supporting Saturn.

We hold that § 46.1-550.5:27 of the Motor Vehicle Dealer Licensing Act, as interpreted by the Commissioner, does conflict with the Federal Arbitration Act, and is preempted by the Supremacy Clause, U.S. Const., Art. VI. Therefore, the proposed arbitration provisions in Saturn's Agreement are enforceable in Virginia, and the Commissioner may not prohibit or discourage use of the nonnegotiable arbitration provision in contracts between Saturn and its Virginia dealers.

II.

"The Supremacy Clause of Art. VI of the Constitution provides Congress with the power to pre-empt state law." *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 368, 106 S. Ct. 1890, 1898, 90 L. Ed. 2d 369 (1986). The Federal Arbitration Act was enacted to promote the enforceability of arbitration agreements and to make arbitration a more viable option to parties weary of the ever-increasing "costliness and delays of litigation." *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 220, 105 S. Ct. 1238, 1242, 84 L. Ed. 2d 158 (1985) (quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 2 (1924)). The Supreme Court has repeatedly recognized the value of arbitration as a means of dispute

resolution, most recently in *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 109 S. Ct. 1917, 104 L. Ed. 2d 526 (1989); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 107 S. Ct. 2332, 96 L. Ed. 2d 185 (1987); and *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 105 S. Ct. 3346, 87 L. Ed. 2d 444 (1985).

The FAA (9 U.S.C. § 2) preempts "conflicting state laws which restrict the validity or enforceability of arbitration agreements." *Supak & Sons Mfg. Co. v. Pervel Indus. Inc.*, 593 F.2d 135, 137 (4th Cir. 1979) (footnote omitted). State laws are subject to preemption not only if they directly contradict federal law, but also if they stand "as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Hines v. Davidowitz*, 312 U.S. 52, 67, 61 S. Ct. 399, 404, 85 L. Ed. 581 (1941); *Schneidewind v. ANR Pipeline Co.*, 485 U. S. 293, 298, 108 S. Ct. 1145, 1150, 99 L. Ed. 2d 316 (1988). The FAA constitutes "a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary." *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24, 103 S. Ct. 927, 941, 74 L. Ed. 2d 765 (1983). The language of the FAA requires that states place no greater restrictions upon arbitration provisions than they place upon other contractual terms. In relevant part, the FAA declares that:

> A written provision in . . . a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

9 U.S.C. § 2. Therefore, with few limitations, if a state law singles out arbitration agreements and limits their enforceability it is preempted.[2]

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[2] An exception to federal pre-emption exists if Congress has overridden the FAA by indicating its intent to preclude waiver of the judicial forum for a particular statutory right. State law in agreement with that Congressional mandate would not contravene the FAA. *See Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. at 627-28, 105 S. Ct. at 3355; *Shearson/American Express, Inc. v. McMahon*, 482 U.S. at 226-27, 107 S. Ct. at 2337-38. Likewise, a state law will not be preempted if it addresses that which the FAA does not. *See Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 109 S. Ct. 1248, 1254-55, 103 L. Ed. 2d 488 (1989).

The Commissioner has argued that Congress has expressed an intent to override the FAA's application to arbitration agreements between automobile manufacturers and dealers in the Dealer's Day in Court Act (DDCA), 15 U.S.C. §§ 1221-1225. We have recently stated that:

> Courts cannot determine whether arbitration agreements are to be enforced by making subjective judgments as to the relative importance of various federal statutes. Rather, Congress must provide clear guidance if it wishes federal courts to refrain from enforcing arbitration agreements when violations of a particular statutory right are alleged.

Gilmer v. Interstate/Johnson Lane Corp., 895 F.2d 195, 203 (4th Cir. 1990). Although we note that the text of the DDCA does not evince clear Congressional intent to override the FAA, we do not decide today whether all DDCA claims may be arbitrated. Even if the DDCA does preclude waiver of a judicial forum for the enforcement of its rights, the Virginia statutes do not mirror that restriction but also preclude some waivers of a judicial forum for the enforcement of non-DDCA claims. The question of whether Congress intended all DDCA claims to be arbitrable may be resolved if and when a dispute under the DDCA arises.

The Commissioner argues that the scope of FAA preemption is limited to laws covering existing arbitration agreements, and does not extend to laws that prohibit or regulate the *formation* of arbitration agreements. We disagree. Although most cases have arisen in the context of existing arbitration agreements, that circumstance does not limit the scope of FAA preemption. Indeed, many courts have at least implicitly recognized a broader scope of FAA preemption. *See, e.g., Medical Development Corp. v. Industrial Molding Corp.*, 479 F.2d 345, 348 (10th Cir. 1973); *Collins Radio Co. v. Ex-Cell-O Corp.*, 467 F.2d 995, 997-98 (8th Cir. 1972).

It is clear that a state may not refuse to enforce and may not revoke an existing arbitration agreement on the ground that the contract did not comply with rules of contract formation applicable only to arbitration provisions. *See Webb v. R. Rowland & Co., Inc.*, 800 F.2d 803, 806-07 (8th Cir. 1986) (violation of statute requiring arbitration provisions to be accompanied by a notice in 10-point type that the contract contains a binding arbitration provision does not render an otherwise valid arbitration agreement unenforceable). It is likewise clear that in passing the FAA, "Congress intended to *foreclose* state legislative attempts to undercut the enforceability of arbitration agreements." *Southland Corp. v. Keating*, 465 U.S. 1, 16, 104 S. Ct. 852, 861, 79 L. Ed. 2d 1 (1984) (emphasis added). To restrict the FAA to existing agreements would be to allow states to "wholly eviscerate Congressional intent to place arbitration agreements 'upon the same footing as other contracts.' " *Southland*, 465 U.S. at 16-17 n.11, 104 S. Ct. at 861 (quoting H. R. Rep. No. 96, 68th Cong., 1st Sess., 1 (1924)). The FAA does not allow a state legislature to

circumvent Congressional intent by enacting special rules to discourage or prohibit the formation of agreements to arbitrate. As noted by the district court, "common sense dictates that a state should not be able to escape its enforcement duties under § 2 by banning the formation of arbitration agreements." 717 F. Supp. at 1150.

We have not discovered a single authority which squarely addresses the issue and adopts the Commissioner's narrow interpretation of the scope of FAA preemption. The First Circuit recently rejected the Commissioner's interpretation in *Securities Indus. Ass'n v. Connolly*, 883 F.2d 1114, 1123-24 (1st Cir. 1989). Our court previously alluded to this issue in *Supak & Sons Mfg. Co. v. Pervel Indus. Inc.*, 593 F.2d 135 (4th Cir. 1979), a case which involved a motion to stay proceedings pending arbitration pursuant to § 3 of the FAA. In deciding whether the parties had agreed to arbitrate, we held that Uniform Commercial Code § 2-207 applied to a written confirmation form containing an arbitration provision not agreed upon by the parties in a prior oral agreement. Thus *Supak* held only that the general rule of contract formation applied to contracts involving arbitration, and that the parties had not agreed to arbitrate the issue involved in that litigation. However, we recognized the possibility that: "§ 2 would preempt a state rule of contract formation which applied only to arbitration clauses and which placed an unreasonable burden on the parties' ability to commit themselves to arbitration." *Id.* at 137. We hold today that § 2 does preempt state rules of contract formation which single out arbitration clauses and unreasonably burden the ability to form arbitration agreements. The district court was correct to hold that

"arbitration agreements may not be burdened with 'conditions on (their) formation and execution . . . which are not part of the generally applicable contract law.' " 717 F. Supp. at 1152 (quoting *Securities Indus. Ass'n v. Connolly*, 703 F. Supp. 146, 153 (D. Mass. 1989)).

III.

Having determined that the scope of the FAA encompasses laws affecting the formation of arbitration agreements, we turn now to the question of whether the FAA preempts the statutes at hand. The Virginia statute primarily at issue provides:

> It is unlawful for any manufacturer, factory branch, distributor or distributor branch, or any field representative, officer, agent or any representative whatsoever of any of them:
>
> * * *
>
> 10. To fail to include in any franchise with a motor vehicle dealer the following language: "If any provision herein contravenes the valid laws or regulations of any state or other jurisdiction wherein this agreement is to be performed, or denies access to the procedures, forums, or remedies provided for by such laws or regulations, such provision shall be deemed to be modified to conform to such laws or regulations, and all other terms and provisions shall remain in full force and effect," or words to that effect.

Va. Code Ann. § 46.1-550.5:27.[3]

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[3] Although the complaint also contests the validity of § 46.1-550.5:24, that provision merely requires the

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Although the statute appears to void all binding arbitration agreements in automobile franchise agreements, we accept as authoritative the Commissioner's interpretation of the statute as forbidding only nonnegotiable arbitration provisions and not negotiable arbitration agreements. Nevertheless, we hold that § 46.1-550.5:27 is preempted to the extent that it places greater restrictions upon arbitration provisions than Virginia places upon other contractual terms. We find that the Commissioner's interpretation conflicts with the FAA because Virginia law generally permits contracting parties to make terms nonnegotiable, and singles out arbitration provisions as an exception to that rule.

The district court held that the statute "does not subject arbitration clauses to burdens not felt by other types of contracts" and indeed "affords privileged status to arbitration agreements," 717 F. Supp. at 1150, but we disagree. We find persuasive the reasoning of *Securities Indus. Ass'n v. Connolly*, 883 F.2d 1114 (1st Cir. 1989), which held that Massachusetts regulations barring securities brokerage firms from including nonnegotiable arbitration provisions in their customer agreements were preempted by the FAA. The Massachusetts regulations (1) made it unlawful for securities brokerage firms to insist

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Commission's [sic] approval of franchise or sales agreements to prevent the formation of agreements containing terms inconsistent with the Motor Vehicle Dealer Licensing Act. Since § 46.1-550.5:24 is essentially an enforcement provision which does not independently pertain to arbitration agreements, it does not conflict with the FAA and is not preempted.

that prospective customers agree to arbitrate future disputes; (2) required brokerage firms to bring this prohibition to the attention of prospective customers who were offered arbitration as an option; and (3) required brokerage firms to explain the legal effect of any arbitration provision offered as an option. Thus, as the statute in this case, the Massachusetts regulations essentially prohibited nonnegotiable arbitration agreements.

The district court did not have before it the First Circuit's opinion, but distinguished the district court's opinion in *Connolly, supra,* 703 F. Supp. 146, in part because the defendants in that case admitted that the regulations in question singled out arbitration agreements. In the present case the state does not concede that the statute singles out arbitration agreements for especially burdensome treatment, but we find that the import of the statute renders it indistinguishable from the *Connolly* regulations.

The Commissioner contends that because the Virginia statute does not mention arbitration, and applies to any contractual provision that denies dealers access to the "procedures, forums or remedies" in Virginia, it does not single out arbitration agreements. He points out that the statute conceivably would void forum-selection provisions. However, the mere fact that a statute or regulation does not expressly refer to arbitration is not determinative on the question of whether it impermissibly singles out arbitration provisions. In *Southland Corp. v. Keating, supra,* the Supreme Court held that a California franchise statute which did not expressly refer to arbitration, but which voided any term that waived its protections, was

preempted to the extent that it had the effect of prohibiting arbitration provisions. Nor is the fact that the Virginia statute voids other contractual provisions determinative, because the Supreme Court has emphasized that the focus should be on whether the statute, either on its face or as applied, imposes burdens on arbitration agreements that do not apply to contracts generally. *See Southland*, 465 U.S. at 16-17 n.11, 104 S. Ct. at 861; *Perry v. Thomas*, 482 U.S. 483, 492-93 n.9, 107 S. Ct. 2520, 2527, 96 L. Ed. 2d 426 (1987).

The district court erred in comparing the instant statute favorably to other provisions of the Motor Vehicle Dealer Licensing Act which absolutely bar the formation of certain terms between automobile manufacturers and dealers; *e.g.*, a manufacturer may not sign a contract with a new dealership within a certain geographic proximity of an existing dealer without notice and a hearing, and it is unlawful for parties to contract in violation of that section. § 46.1-550.5:27(4). From similar sections, the lower court reasoned that arbitration clauses are favored under the Motor Vehicle Dealer Licensing Act because only with respect to those provisions may the parties agree to "an otherwise *impermissible* term." 717 F. Supp. at 1151 (emphasis added). The lower court's analysis is flawed because it implies that a state may categorize arbitration agreements with other specific contractual terms which are void because they violate public policy – a hypotheses clearly contrary to the FAA.

Thus, the chief error in the district court's analysis is that it fails to use an appropriate comparison group. In determining whether the Virginia statute impermissibly burdens arbitration provisions, it must be compared to

general contract law rather than to laws which apply only to contracts subject to the Motor Vehicle Licensing Act, or to miscellaneous statutes which prohibit a narrow assortment of unrelated contractual terms because they violate public policy.[4] The fact that the statute at issue might affect other terms in dealership agreements does not save it from preemption. As emphasized by the Supreme Court in *Southland*, 465 U.S. at 16-17 n.11, 104 S. Ct. at 861, only those grounds "that [exist] at law or in equity 'for the revocation of *any* contract' " are legitimate defenses to the enforceability of arbitration provisions. The essential difference between the regulations in *Connolly* and the U.C.C. provision at issue in *Supak & Sons Mfg. Co. v. Pervel Indus. Inc., supra*, is that the former are targeted at arbitration agreements whereas the latter is "a general rule of contract formation." *Supak*, 593 F.2d at 137.

Thus, in determining whether this statute forms an idiosyncratic rule specific to arbitration agreements or whether it is merely an unremarkable part of Virginia's general laws of contract formation, we must compare it with general common law and statutory law. The statute at issue, like the regulations in *Connolly*, impact arbitration agreements by forbidding their formation as

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[4] Ironically, the district court faulted *Connolly* for what it perceived as a similar error, because it believed that the district court in *Connolly* erroneously compared the Massachusetts regulations only to the body of state common law, unenhanced by statutory law. *See Connolly*, 703 F. Supp. at 153. We read the First Circuit opinion as including in the comparative body of law both general principles of common law and of statutory law.

nonnegotiable contractual terms. The statute is clearly intended to avoid potentially adhessive arbitration contracts between automobile manufacturers and dealers. If Virginia uniformly barred the formation of nonnegotiable contractual terms or declared all contracts of adhesion to be presumptively unenforceable, then the statute at issue would not be at odds with general contract law. *See Connolly*, 883 F.2d at 1120-21. However, as a general rule, Virginia does not bar parties from making certain provisions of their contracts nonnegotiable.[5] In fact, no other Virginia statute requires that a nonnegotiable provision in a standardized contract be made optional. In addition, Virginia does not always, or even usually, presume adhesive contracts to be unenforceable. Instead, Virginia adheres to the general rule that: "The use of a standard form contract between two parties of admittedly unequal bargaining power does not invalidate an otherwise valid contractual provision. To be invalid, the provision at issue must be unconscionable." *Webb v. R. Rowland & Co., Inc.*, 800 F.2d at 807.

The FAA does not permit a state to single out arbitration agreements in standardized contracts and, in effect, declare their very formation to be unconscionable.

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[5] The district court noted that certain provisions of the Insurance Code, the Beer Franchise Act, the Retail Franchising Act, the Petroleum Products Franchise Act, and other miscellaneous provisions of the Virginia Code, like the Motor Vehicle Dealer Licensing Act, also flatly prohibit certain terms without opportunity for negotiation. However, specialized provisions applicable only to certain types of contracts do not form a cohesive general law or pattern of laws applicable to most contracts.

Requiring arbitration provisions in dealership agreements to be optional rather than nonnegotiable unreasonably burdens the formation of arbitration agreements. If Saturn could not require that Virginia dealers agree to arbitration, it could be forced to contract with dealers who agree to all provisions except arbitration, despite the fact that arbitration is a core provision of Saturn's Dealership Agreement.[6] The Federal Arbitration Act does not allow such singular hostility to the formation of arbitration agreements. Because it has no general contract law restricting nonnegotiable provisions in standardized contracts, Virginia may not bar automobile manufacturers from making arbitration provisions a nonnegotiable term of doing business.

Thus, we hold that the statute is preempted because, as in *Southland*, it treats arbitration agreements more harshly than other contracts by disallowing their formation as mandatory provisions. "[C]ourts must be on guard for artifices in which the ancient suspicion of arbitration might reappear." *Connolly*, 883 F.2d at 1119. Since the Virginia statute resembles the regulations in *Connolly* more than the general rule of contract formation in *Supak*, we hold that it is preempted to the extent that it affects arbitration agreements.

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[6] It is important to keep in mind that no automobile dealer is required to contract with the plaintiff. This is a new company, a new product, and a new concept of marketing. Dealers are not required to execute the new agreement in order to continue as dealers under existing conditions. It is only dealers wishing to sell the Saturn automobile who are required to agree to arbitration.

IV.

Our holding today reflects our disagreement with the notion adopted by the district court that the Virginia statute may be harmonized with the FAA because it only ensures "consensual rather than forced arbitration." Both the district court and the Commissioner cite portions of testimony taken at the legislative hearings on the FAA, which suggest that some advocates of the bill did not anticipate that it would be applied to certain standardized contracts. That these early remarks should not be over-emphasized is evident both from the absence of limiting language in the FAA and from the fact that the Act has often been applied to standardized contracts. *See, e.g., Rodriguez de Quijas*, 109 S. Ct. at 1918 (standardized contract between securities broker and its customers); *Mitsubishi*, 473 U.S. at 617, 105 S. Ct. at 3349 (standardized franchise agreement between automobile manufacturer and dealers); *Perry v. Thomas*, 482 U.S. at 485 (standardized contract between securities broker and its employees). *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 109 S. Ct. 1248, 103 L. Ed. 2d 488 (1989), is not to the contrary. In *Volt*, 109 S. Ct. at 1255, the Supreme Court stated that "[a]rbitration under the Act is a matter of consent, not coercion;" however, the Court did not intimate that standardized provisions are excluded from the FAA. Rather, the Court's language reflects its focus on the issue in that case – that parties are entitled to incorporate state law restrictions into their arbitration agreement that would otherwise be preempted by the FAA. The Court's statement that arbitration under the FAA is a matter of consent stresses only

that the Act does not impose terms of arbitration but instead leaves them to the agreement of the parties.

The Commissioner contends that the Virginia statute merely prevents coercive agreements, and cites the disparity of bargaining power between manufacturers and dealers. Saturn counters that any disparity in bargaining power is less than most dealer/manufacturer agreements, since Saturn is new and seeks well-established dealers. Regardless of which version is closer to the truth, the FAA simply does not permit a state to legislate policy concerns in such a way as to thwart Congress' intent to place arbitration agreements on equal footing with other contracts. The argument that the Virginia statute is a necessary part of the state's scheme to protect dealers must therefore fail. Similar arguments have been rejected by the Supreme Court in *Southland, supra* (preempting statute designed to provide special protection for franchisees), and in *Perry v. Thomas, supra* (preempting statute designed to protect employees who might sign away in advance their rights to a judicial forum).

It is not this court's function to resolve the question of whether a particular arbitration agreement has been induced by an overwhelming disparity in economic power. However, we note in passing that the mere fact that Saturn requires dealers to agree to its arbitration provisions in order to obtain a Saturn dealership does not make its Dealership Agreement non-consensual. If a dealer does not wish to agree to nonnegotiable arbitration provisions, the dealers need not do business with Saturn. The Commissioner's fears that Saturn's arbitration provisions will be used to force dealers to waive the protections given to them by Virginia law are premature.

Existing Virginia law can and should be applied to revoke *any* contract which results from fraud or the sort of *overwhelming* economic power which can render an agreement unconscionable. *See Rodriguez de Quijas*, 109 S. Ct. at 1921.

V.

For the reasons set forth herein, we reverse the district court's grant of summary judgment to the Commissioner, and we grant summary judgment to Saturn. The challenged provision of the Virginia Motor Vehicle Dealer Licensing Act is preempted by the Federal Arbitration Act to the extent that it interferes with the nonnegotiable arbitration provision contained in Part One, Article 5 of the Automobile Dealership Agreement of plaintiff. Neither the Commissioner nor his agents shall take any act to prevent or discourage the use and/or enforcement of the contractual terms in contracts between Saturn Distribution Corporation and its dealers in the Commonwealth of Virginia requiring the exclusive use of binding arbitration for the determination of dealer contract disputes.

REVERSED

WIDENER, Circuit Judge, dissenting:

In my opinion, the majority abandons the proper and appropriate preemption analysis and fails to take account of Virginia's inherent right to protect her own citizens. Therefore, I respectfully dissent.

The various circumstances under which a federal statute may, by virtue of the supremacy clause, preempt state law are well settled: "when Congress . . . expresses a

clear intent to preempt state law, when there is outright or actual conflict between federal and state law, where compliance with both federal and state law is in effect physically impossible, where there is implicit in federal law a barrier to state regulation, where Congress has legislated comprehensively, thus occupying an entire field of regulation and leaving no room for the States to supplement federal law, or where the state law stands as an obstacle to the accomplishment and execution of the full objectives of Congress." *Louisiana Public Service Comm'n v. FCC*, 476 U.S. 355, 368-69 (1986) (citations omitted). It is at once apparent that the preemption varieties just mentioned are not equals, although the preemptive effect is the same if a category applies, but a sliding scale in which a finding of preemption becomes more difficult as the tension between state and federal enactments becomes more obscure.

The category of preemption the majority employs here, the "frustrate the federal policy" theory, 476 U.S. at 369, rests at the bottom of this scale because "preemption under a frustration of federal purpose theory is more an exercise of policy choices by a court than strict statutory construction. An independent judgment that federal purposes require preemption comes in the face of congressional silence, both express and implied, on the subject." *Abbot v. American Cyanamid Co.*, 844 F.2d 1108, 1113 (4th Cir.), *cert. denied*, 57 U.S.L.W. 3280 (1988). In the face of Congressional silence, "there is a presumption against preemption." *Abbot*, 844 F.2d at 1112. Moreover, because statutes that regulate the relationship between dealers and manufacturers in an attempt to equalize the parties' respective bargaining power are a legitimate exercise of a

state's police powers, *Boatland, Inc. v. Brunswick Corp.*, 558 F.2d 818, 823 (6th Cir. 1977), " 'we start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.' " *California v. ARC America Corp.*, 57 U.S.L.W. 4425, 4427 (1989) (quoting *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947)).

Therefore, the appropriate starting point in examining the statute in question is not a "liberal federal policy favoring arbitration agreements," as the majority would have it. Every federal statute presumably was enacted to further a strong or liberal federal policy in favor of or against something, but that does not lead inexorably to preemption of every state law that touches on the same subject matter. *See Pacific Gas & Elec. Co. v. State Energy Resources Conservation & Dev. Comm'n*, 461 U.S. 190 (1983) (upholding state moratorium on construction of new nuclear power plants despite federal policy promoting nuclear power); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981) (upholding state's coal severance tax despite federal policy favoring production and use of coal); *see also* L. Tribe, *American Constitutional Law* § 6-26, at 488 (1988) ("state laws that merely push against the grain of 'general expressions of national policy' in federal statutes will not, for that reason alone, be deemed to be preempted"). Instead, the proper analytical starting point is the presumption, double strength in this case to be sure, against preemption absent a clear and manifest Congressional intent to the contrary.

Applying the preceding principles to the Virginia statute is neither difficult nor lengthy, and requires a different decision than the majority obtains. First, "[t]he

FAA contains no express pre-emptive provision, nor does it reflect a congressional intent to occupy the entire field of arbitration." *Volt Information Sciences, Inc. v. Board of Trustees*, 57 U.S.L.W. 4295, 4298 (1989). To support a finding of preemption, therefore, the Virginia statute must in some way directly conflict with the FAA.

Because the FAA "[b]y its terms, does not apply until the arbitration clause in question is determined to be part of the contract," *Supak & Sons Mfg. Co. v. Pervel Indus.*, 593 F.2d 135, 137 (4th Cir. 1979), virtually every reported case in which a court has determined that the FAA preempts state law has dealt with the *enforceability of otherwise* valid arbitration agreements. The Virginia statute in issues deals not with the enforceability of arbitration agreements, however, but with their formation. As interpreted by the Commissioner, the statute only precludes Saturn from unilaterally imposing agreements to arbitrate upon its dealers. If a dealer agrees to arbitrate, the Virginia statute is no impediment to the agreement's enforceability. Because there is no direct conflict between the state statute and the FAA, this should end the inquiry under a proper preemption analysis. Because I believe the majority also errs by failing to recognize the significance of the Dealer's Day in Court Act (DDCA), 15 U.S.C. §§ 1221-1225, however, I will address that issue.

The majority recognized that "[a]n exception to federal preemption exists if Congress has overridden the FAA by indicating its intent to preclude waiver of the judicial forum for a particular statutory right." Slip op. at 7, n.2. Although refusing to decide whether DDCA claims may be arbitrated, the majority notes that "the DDCA

does not evince clear Congressional intent to override the FAA. . . . " I disagree.

A Congressional intent to preclude waiver of a judicial forum for a particular statutory right "will be deducible from text or legislative history." *Mitsubishi Motors v. Soler Chrysler-Plymouth*, 473 U.S. 614, 628 (1985). The legislative history of the DDCA, written some thirty years after the FAA was enacted in 1925, could not be more clear: "The bill creates a cause of action where none previously existed in that, *irrespective of contractual provisions*, it grants a right of review in the Federal courts of disputes between automobile manufacturers and their dealers. . . . " H.R. Rep. No. 2850, 84th Cong., 2d Sess., *reprinted in* 3 U.S. Code Cong. & Ad. News 4596, 4596 (1956) (italics added); *see Blenke Brothers Co. v. Ford Motor Co.*, 217 F. Supp. 459, 463-64 (N.D. Ind. 1963) (dealer may pursue DDCA claim despite failing to comply with contractual provision requiring notice to defendant's Dealer Policy Board).

Perhaps mindful of the DDCA's legislative history, the majority declines to decide "whether all DDCA claims may be arbitrated." Instead, the majority invalidates the Virginia statute because it "also preclude[s] some waivers of a judicial forum for the enforcement of non-DDCA claims." In my view, this both mischaracterizes the Virginia statute and understates the significance of the DDCA's legislative history.

First, as noted earlier, the Virginia statute not only does not preclude waiver of a judicial forum for non-DDCA claims, it does not preclude waiver of a judicial forum for any claim. The statute merely ensures that, if a

waiver occurs, the waiver is a voluntary choice on the part of the dealer and is not extracted by the manufacturer as part of a nonnegotiable contract of adhesion.

Second, the DDCA in terms supplies an automobile dealer with an action for the failure of an automobile manufacturer "to act in good faith in performing or complying with any of the terms or provisions of the franchise, or in terminating, canceling, or not renewing the franchise." 15 U.S.C. § 1222. This broad private action, which could extend to disputes over every aspect of the franchise relationship, was enacted for much the same reasons as the Virginia statute:

> Concentration of economic power in the automobile manufacturing industry of the United States has developed to the point where legislation is required to remedy the manifest disparity in the ability of franchised dealers of automotive vehicles to bargain with their manufacturers. . . . The bill as amended proceeds from the conclusion that in the automobile industry concentration of economic power has increased to the degree that traditional contractual concepts are no longer adequate to protect the automobile dealers under their franchises.

H.R. Rep. No. 2850, 3 U.S. Code Cong. & Ad. News at 4596-97. Moreover, the DDCA explicitly does not preempt state law on the subject unless there is an express and direct conflict between state and federal statutes. 15 U.S.C. § 1225.

Because Congress has expressed a clear intent to preclude a contractual requirement of waiver of a judicial forum for DDCA claims, the fact that the DDCA might

not encompass every conceivable claim between manufacturer and dealer is of no consequence. I believe the DDCA is directly relevant not only to whether an exception to preemption exists, but, especially under a "frustrate the federal policy" theory, to whether preemption should apply in the first instance. Thus, the paramount question is revealed as not whether the DDCA immunizes a presumptively suspect state statute, but whether Congress has expressed a clear intent to preempt a presumptively valid state statute. Not only does the FAA fail to manifest such intent, but the DDCA, enacted thirty years after the FAA to advance exactly the same interests as the Virginia statute, appears to go even further than does the state statute. I believe that, if the most that can be said, as here, is that a presumptively valid state statute is in general tension with a federal statute of general application, and yet furthers precisely the same goals as another federal statute dealing with the specific subject in issue, the state enactment should stand until Congress says otherwise.

At bottom, the majority opinion rests on the one case in which a court determined that a state rule prohibiting unilateral imposition of arbitration agreements was preempted by the FAA, *Securities Indus. Ass'n v. Connolly*, 883 F.2d 1114 (1st Cir. 1989). Even if we assume the FAA may preempt state rules of contract formation (an assumption with which it is at once apparent I do not agree),[1] *Connolly* is unpersuasive for at least two reasons.

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[1] The Eleventh Circuit has adhered to the FAA's distinction between contract formation and contract enforcement

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First, the underlying reasoning of *Connolly* is its concern with "[i]ncreased resort to the courts, and the consequent tumefaction of already-swollen court calenders," 883 F.2d at 1116, a consideration I think is impermissible in view of Article III's command that Congress establish our jurisdiction. As well, *Connolly* relegates Massachusetts' regulation of arbitration agreements for "the public weal" as "self-congratulatory casuistry [that] will not wash." 883 F.2d at 1120. Such reliance, I suggest, only reveals the weakness of the position.

More to the point, *Connolly* is a securities case, and securities regulation is one area in which the Supreme Court has addressed the effect of the FAA. *See Rodriguez de Quijas v. Shearson/American Express, Inc.*, 57 U.S.L.W. 4539 (1989); *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987). Thus, although I disagree with the *Connolly* court's analysis, it is at least understandable that, in light of Supreme Court precedent, that court found that "nothing in the Securities Act, the Exchange Act, or the grant of concurrent power to the states to regulate securities manifests a congressional intent to limit or prohibit waiver of a judicial forum . . . or to abridge the sweep of the FAA." *Connolly*, 883 F.2d at 1121. Even on that basis, however, the result the majority

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even though the state rule of formation singled out arbitration clauses for somewhat less favorable treatment. *See Eassa Properties v. Shearson Lehman Brothers*, 851 F.2d 1301, 1304 n.7 (11th Cir. 1988) (upholding provision of Uniform Partnership Act which provided that all partners must agree to submit claim or liability to arbitration). I advocate, of course, that we should agree with *Eassa* rather than with *Connolly*.

obtains here is not warranted. By contrast, the Virginia statute arises not from a grant of concurrent power, but from the State's inherent police power, and Congress in the DDCA did manifest an intent to preclude waiver of a judicial forum for claims between automobile dealers and manufacturers.

Virginia has determined, as did Congress, that a manifest disparity in bargaining power exists between automobile dealers and their manufacturers. By precluding Saturn from making arbitration clauses nonnegotiable, Virginia is merely seeking to ensure that arbitration "is a matter of consent, not coercion. . . . "[2] *Volt Information Sciences, Inc. v. Board of Trustees*, 57 U.S.L.W. 4295, 4298 (1989). Although Congress may have enacted the FAA to "revers[e] centuries of judicial hostility to arbitration agreements," *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 510 (1974) (footnote omitted), I cannot believe that our federalism will tolerate replacing judicial hostility with judicial advocacy. We sit, after all, to do justice between man and man and citizen and sovereign, not to keep our dockets clear.

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[2] I take cold comfort in the majority's "important" recognition of the fact that "no automobile dealer is required to contract with [Saturn]." Slip op. at 16, n.6. No one is required in the legal sense to execute any contract of adhesion, or by definition a contract would not exist, yet that does not prevent courts and legislatures from designating certain contracts as adhesive. Moreover, it is equally true that General Motors is not required to sell Saturn automobiles in Virginia, as the Court indicated was the case with Audis or Volkswagens in *World Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286, 287 (1980).

Appendix B

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA

Richmond Division

SATURN DISTRIBUTION CORPORATION, Plaintiff, v. DONALD E. WILLIAMS, Commissioner of the Department of Motor Vehicles, Commonwealth of Virginia, Defendant, and VIRGINIA AUTOMOBILE DEALERS ASSOCIATION, INC., Intervenor.	Civil Action No. 89-319-R (Filed August 17, 1989)

MEMORANDUM OPINION

The plaintiff in this case is suing for a declaratory judgment that § 46.1-550.5:27(10) of the Code of Virginia, as interpreted by the Commissioner of Motor Vehicles is preempted by Section 2 of the Federal Arbitration Act, 9 U.S.C. § 2. The parties agree that there are no issues of material fact in dispute, and have submitted opposing motions for summary judgment pursuant to Rule 56 of the Federal Rules of Civil Procedure.

Background

The plaintiff, Saturn Distribution Corporation, is a wholly-owned subsidiary of Saturn Corporation, which is, in turn, a wholly-owned subsidiary of General Motors Corporation. Saturn was created in 1985 to design, manufacture and market a new model of car. In so doing, it adopted what it calls a new "Mission and Philosophy" of manufacturing and marketing cars, including a determination "to further the spirit of trust and respect which is critical to the relationship" between Saturn and its dealers. *Saturn Distribution Corporation Dealer Agreement*, at 1 (hereinafter "Dealer Agreement"). In order to promote this new Mission and Philosophy and further cooperation, Saturn developed an alternative dispute resolution system, including binding arbitration,[1] and made it a mandatory part of the Dealer Agreement.[2]

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[1] The system involves two steps, the first of which involves nonbinding mediation. If the claim is not resolved by mediation, it may then be submitted to binding arbitration. Both the mediation and the arbitration panels are to consist of two dealers and two Saturn representatives, and are expected to reach a consensus solution. *Dealer/Saturn Dispute Resolution Guide*, at 14-20.

[2] The relevant language is found in Article 5 of the Dealer Agreement:

> [Saturn] and Dealer acknowledge that, at the state and federal levels, various courts and agencies would, in the absence of this Article 5, be available to them to resolve claims or controversies which might arise between them. [Saturn] and Dealer agree that it is inconsistent with the Mission and Philosophy for either to use courts or governmental agencies to resolve such claims or controversies.

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The Virginia Motor Vehicle Dealer Licensing Act, Va. Code Ann. §§ 46.1-515 et seq., was enacted to protect automobile dealers from the imbalances in bargaining power inherent in their relationships with automobile manufacturers. Section 46.1-550.5:27(10) states that an automobile distribution agreement must contain language identical in effect to the following:

> If any provision herein contravenes the valid laws or regulations of any state or other jurisdiction wherein this agreement is to be performed, or denies access to the procedures, forums, or remedies provided for by such laws or regulations, such provision shall be deemed to be modified to conform to such laws or regulations, and all other terms and provisions shall remain in full force and effect.

Section 46.1-550.5:24 requires that distributors submit franchise agreements to the Commissioner of Motor Vehicles for approval.

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THEREFORE, CONSISTENT WITH THE PROVISION OF THE UNITED STATES ARBITRATION ACT (9 U.S.C. Section 1 et seq.), DEALER AND [SATURN] AGREE THAT THE DISPUTE RESOLUTION PROCESS OUTLINED IN THIS ARTICLE, WHICH INCLUDES BINDING ARBITRATION, SHALL BE THE EXCLUSIVE MECHANISM FOR RESOLVING ANY CONTROVERSY OR CLAIM BETWEEN THEM ARISING OUT OF OR RELATING TO THIS AGREEMENT, ITS CREATION, OR TERMINATION.

Dealer Agreement, at 3.

Defendant Donald E. Williams is Commissioner of the Department of Motor Vehicles. When Saturn submitted its agreement, containing the exclusive arbitration clause, to him, he refused to approve it. He stated that he would, however, approve an agreement that gives the dealer the option to delete the exclusive arbitration clause. He made it clear that this did not mean that Saturn would be prohibited from including an arbitration clause in its agreement. Rather, Saturn would not be permitted to make the inclusion of the arbitration clause a prerequisite to becoming a Saturn dealer.[3] The Commissioner informed Saturn that it would be able to develop, on its own, a method of explaining to potential dealers that they had the option to accept or reject the arbitration clause in their agreements.

Saturn is now suing under the Supremacy Clause, U.S. Const., art. 6, claiming that § 46.1-550.5:27(10) is preempted by § 2 of the Federal Arbitration Act (FAA), 9 U.S.C. § 2. That section reads:

> A . . . contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole

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[3] The Commissioner notes that he could have chosen to interpret § 46.1-550.5:27(10) as forbidding even bargained-for arbitration clauses, but that such an interpretation would clearly conflict with federal policies favoring voluntary arbitration. Instead, he has chosen the more flexible interpretation that such clauses are acceptable if the dealer has the option to reject them. This interpretation should be accepted as authoritative. *Hoffman Estates v. Flipside, Hoffman Estates Inc.*, 455 U.S. 489, 494 n.5 (1982).

> or any part thereof . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Saturn requests a declaratory judgment stating that § 46.1-550.5:27(10) as applied by the Commissioner to Saturn's agreement is preempted by § 2 of the FAA, and that the exclusive arbitration provision of Saturn's agreement is valid, as well as a permanent injunction prohibiting the Commissioner from preventing or discouraging the use or enforcement of exclusive arbitration clauses between Saturn and its dealers.

The Virginia Automobile Dealers Association (VADA) is a trade association representing six hundred new car and truck dealers in Virginia. On June 27, 1989, VADA sought, and the Court granted, leave to intervene as a defendant in this case.

Discussion

The defendant and intervenor first argue that this Court does not have subject matter jurisdiction of this case. The Supreme Court has ruled that Supremacy Clause challenges to state laws present federal questions under 28 U.S.C. § 1331. *Shaw v. Delta Airlines*, 463 U.S. 85, 96 n.14 (1983). This Court therefore properly has jurisdiction of this case.

In order to prevail on its preemption argument, the plaintiff must demonstrate that the Virginia statute, as interpreted by the Commissioner, "stands as an obstacle to the accomplishment and execution of the full purposes and objectives" of the Federal Arbitration Act. *Hines v.*

Davidowitz, 312 U.S. 52, 67 (1941), quoted in *Volt Information Sciences v. Board of Trustees*, ___ U.S. ___, 103 L.Ed.2d 488, 499 (1989). The FAA was enacted to ensure that agreements to arbitrate would be enforced in court " 'upon the same footing as other contracts.' " *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 219 (1985), quoting H.R. Rep. No. 96, 68th Cong., 1st Sess. 1 (1924). " '[T]he purpose of the act was to assure those who desired arbitration and whose contracts related to interstate commerce that their expectations would not be undermined by federal judges or by state courts or legislatures.' " *Southland Corp. v. Keating*, 465 U.S. 1, 13 (1984), quoting *Metro Industrial Painting Corp. v. Terminal Construction Co.*, 287 F.2d 382, 387 (2d Cir. 1961); *accord Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 10 (1983). Indeed, on all previous occasions in which the FAA has come before the Supreme Court, it was in the context of the enforceability of an existing arbitration agreement. *See, e.g., Rodriguez de Quijas v. Shearson/American Express*, 104 L.Ed.2d 526 (1989); *Volt Information, supra; Shearson/American Express v. McMahon*, ___ U.S. ___, 96 L.Ed.2d 185 (1987); *Perry v. Thomas*, ___ U.S. ___, 96 L.Ed.2d 426 (1987); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985); *Byrd, supra; Southland, supra; Moses H. Cone, supra; Scherk v. Alberto-Culver*, 417 U.S. 506 (1974); *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395 (1967).

Although the primary purpose of the FAA is to ensure the enforceability of arbitration agreements, common sense dictates that a state should not be able to escape its enforcement duties under § 2 by banning the formation of arbitration agreements. The Fourth Circuit

recognized this principle in *Supak & Sons Mfg. Co., Inc. v. Pervel Industries, Inc.*, 593 F.2d 135 (4th Cir. 1979). Although *Supak* held that § 2 "does not displace state law on the general principles governing formation of the contract itself," it also stated:

> Perhaps, although we do not decide the point, § 2 would preempt a state rule of contract formation which applied only to arbitration clauses and which placed an unreasonable burden on the parties' ability to commit themselves to arbitration.

Id. at 137; *see also Perry*, 96 L.Ed.2d at 437, n.9 ("A state law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with . . . § 2."). The plaintiff in the present case argues that § 46.1-550.5:27(10) is preempted by the FAA because it singles out arbitration clauses and subjects only such clauses to the opt-out treatment.

The Virginia statute does not subject arbitration clauses to burdens not felt by other types of contracts. In fact, an overview of the law of Virginia that governs the formation of contracts reveals that § 46.1-550.5:27(10), as interpreted by the Commissioner, affords privileged status to arbitration agreements. Other provisions of the Virginia Motor Vehicle Dealer Licensing Act, not to mention the Insurance Code, Va. Code §§ 38.2-100 et seq., the Beer Franchise Act, *id.* §§ 4-118.3 et seq., the Wine Franchise Act, *id.* §§ 4-118.42 et seq., the Retail Franchising Act, *id.* §§ 13.1-557 et seq., the Petroleum Products Franchise Act, *id.* §§ 59.1-21.8 et seq., as well as provisions governing sports agents contracts, *id.* §§ 18.2-501.1 et

seq., and preneed funeral contracts, *id.* § 54.1-2820, dictate the form of certain types of contracts, with no opportunity whatsoever for negotiation.

In the case of the Motor Vehicle Dealer Licensing Act, for example, the manufacturer may not prevent the sale or transfer of the dealership without notice to the dealer and, if requested, a hearing before the Commissioner, § 46.1-550.5:27(3), nor may it sign a contract with a new dealership within a certain geographic proximity to an existing dealer, without notice and a hearing. § 46.1-550.5:27(4). It is unlawful to include provisions in a franchise agreement that violate these sections. § 46.1-550.5:27(9).[4] The Commissioner has not interpreted § 46.1-550.5:27(9) to allow the parties to give evidence, in the form of opt-out language, that they have negotiated and agreed to a provision that violates one of these sections. It is simply unlawful to include such a provision. Only with respect to arbitration clauses does the Commissioner allow the parties to negotiate to include an otherwise impermissible term. Section 46.1-550.5:27(10) does not, therefore, single out arbitration agreements for special treatment that "burden[s] . . . the parties' ability to commit themselves to arbitration," *Supak*, 593 F.2d at 137. Rather, among the plethora of Virginia laws designed to govern the formation of various types of contracts, it grants a flexibility not permitted with respect to any other type of provision.

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[4] The Fourth Circuit has held that the predecessor to the statute presently at issue does not violate the commerce clause or the due process clause. *American Motors Sales Corp. v. Department of Motor Vehicles*, 592 F.2d 219 (1979); *see also New Motor Vehicle Board v. Orrin W. Fox Co.*, 439 U.S. 96 (1978).

Section 46.1-550.5:27(10), as interpreted by the Commissioner, in no way "stands as an obstacle to the accomplishment and execution of the full purposes and objectives," *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941), of the Federal Arbitration Act. Arbitration, in order to be legitimate, must result from the acquiescence of both parties; it may not be imposed by one party upon the other. A New York state court has noted that

> arbitration is consensual in nature. The fundamental assumption of arbitration is that it may be invoked as an alternative to the settlement of disputes through the judicial process "solely by reason of an exercise of choice by [all] parties."

Miner v. Walden, 101 Misc. 2d 814, 422 N.Y.S. 2d 335, 337 (N.Y.Sup. Ct. 1979), quoting Henderson, *Contractual Problems in the Enforcement of Agreements to Arbitrate Medical Malpractice*, 58 Va. L. Rev. 947, 985 (1972); *see also Domke on Commercial Arbitration* at 1 (1988). A colloquy that occurred during the 1923 hearings on the proposed FAA indicates that several of the proponents of the bill did not envision that it would be applied to contracts of adhesion, but rather to voluntary agreements among merchants. Hearings on S.4213 and S.4214 Before the Subcommittee of the Committee on the Judiciary, 67th Cong., 4th Sess. 9-11 (1923). The Supreme Court also acknowledged this principle when it stated that, "Arbitration under the Act is a matter of consent, not coercion." *Volt Information*, 103 L.Ed.2d at 500. By ensuring consensual rather then forced arbitration, the Virginia statute is entirely in harmony with the Federal Arbitration Act.[5]

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[5] Considering the glowing terms in which the plaintiff's attorneys, briefs and documents all describe Saturn's new

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The plaintiffs cite two appellate court cases and one recent district court case in support of their motion. *Collins Radio Co. v. Ex-Cell-O Corp.*, 467 F.2d 995 (8th Cir. 1972), *Webb v. R. Rowland & Co., Inc.*, 800 F.2d 803 (8th Cir. 1986), and *Securities Industry Ass'n v. Connolly*, 703 F.Supp. 146 (D.Mass 1988). *Collins Radio* and *Webb* are both easily distinguishable from the present case, as both involved existing agreements to arbitrate, which the Eighth Circuit held enforceable in accordance with the dictates of § 2. In addition, the state statutes at issue in those two cases very explicitly singled out arbitration agreements, with one requiring the acknowledgment of an attorney for each party that his client has been advised of the ramifications of agreeing to arbitrate, *Collins Radio*, 467 F.2d at 997, and the other requiring arbitration clauses to be introduced by a notice, in ten-point capital letters. *Webb*, 800 F.2d at 805. As explained above, the statute challenged in the present case does not single out arbitration clauses for such special treatment, but rather forms part of an overall program of regulation of potentially adhesive contracts.

Connolly is the only other preemption case under the FAA in which the plaintiffs were seeking the invalidation of a state law regulating the formation of arbitration agreements, rather than the enforcement of an existing

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Mission and Philosophy, the Court rests easy in the knowledge that the plaintiff should have little need for the coercion for which it is fighting here, but instead will easily persuade its new dealers to consent voluntarily to its dispute resolution process.

arbitration agreement. The Massachusetts regulations challenged in *Connolly* prohibited broker-dealers from making an arbitration agreement a prerequisite for opening an account, and required broker-dealers to disclose the legal effect of such an agreement. *Id.*, 703 F.Supp. at 148-49. These regulations are, with respect to the first of these provisions, similar to the statute at issue in the present case, in that they basically prohibit adhesive arbitration agreements. Judge Woodlock held that the state regulations were preempted

> [b]ecause the voluntariness concerns expressed in the unique Massachusetts securities arbitration regulations impose conditions on the formation and execution of arbitration agreements which are not part of the generally applicable contract law of Massachusetts . . .

Id. at 153.

The present case is distinguishable from *Connolly*. The defendants in that case admitted that the regulations in question singled out arbitration agreements. *Id.*, 703 F.Supp. at 152. In view of the dicta in *Perry* that "[a] state law principle that takes its meaning precisely from the fact that a contract to arbitrate is at issue does not comport with . . . § 2," 96 L.Ed.2d at 437, n.9, the Massachusetts court could not but hold that the regulations were preempted by the FAA. The defendant in this case does not make this concession, and this Court has agreed, *supra*, that the statute here at issue does not single out arbitration agreements for especially burdensome treatment.

Furthermore, while this Court agrees that arbitration agreements may not be burdened with "conditions on

[their] formation and execution . . . which are not part of the generally applicable contract law," *Connolly*, 703 F.Supp. at 153, it does not agree with the result reached by the Massachusetts court. Judge Woodlock, in holding that the regulations were preempted, stated that they "represent[ed] a radical departure from the treatment of contracts generally in the State's common law." *Id.* He acknowledged that "Massachusetts law does contain a variety of idiosyncratic statutory provisions which require special treatment of – and disclosure regarding – certain types of contractual provisions," but wrote these off as "the exceptions that prove the rule." *Id.* It appears that, underlying the holding in *Connolly* is the premise that the body of law governing the formation of contracts generally which may constitutionally be applied to arbitration agreements should be limited to the state's common law, unenhanced by statutory law. This Court does not take such a restricted view, but instead believes that this body of law should consist of all statutory and common law that governs the formation of contracts. This approach finds support in *Supak*, 593 F.2d 135, in which the Fourth Circuit held that Uniform Commercial Code provisions governing the formation of contracts applied to invalidate an arbitration clause.

Because § 46.1-550.5:27(10) does not single out arbitration agreements for special treatment, but rather forms an unexceptional part of the law of Virginia applicable to the formation of contracts, and because the effect that it has on arbitration agreements does not "stand[] as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," the statute is not preempted by § 2 of the Federal Arbitration Act. The

plaintiff's motion is DENIED, the defendant's and intervenor's motions are GRANTED, and judgment is entered in their favor.

It is so ORDERED.

Let the Clerk send a copy of this Order to all counsel of record.

AUG 17 1989
DATE

/s/ Richard L. Williams
UNITED STATES DISTRICT JUDGE

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF VIRGINIA

Richmond Division

SATURN DISTRIBUTION CORPORATION, Plaintiff, v. DONALD E. WILLIAMS, Commissioner of the Department of Motor Vehicles, Commonwealth of Virginia, Defendant, and VIRGINIA AUTOMOBILE DEALERS ASSOCIATION, INC., Intervenor.	)	Civil Action No. 89-319-R (Filed August 17, 1989)

FINAL ORDER

This matter is before the Court on the cross motions for summary judgment pursuant to Rule 56 of the Federal Rules of Civil Procedure.

For the reasons set forth in the accompanying memorandum opinion, the motions of defendant Williams and intervenor Virginia Automobile Dealers Association are GRANTED, and judgment is hereby ENTERED in their favor. The plaintiff's motion is hereby DENIED.

It is so ORDERED. Let the Clerk send a copy of this Order to all counsel of record.

AUG 17 1989
DATE

/s/ Richard L. Williams
UNITED STATES DISTRICT JUDGE

Appendix C

UNITED STATES COURT OF APPEALS

FOR THE FOURTH CIRCUIT

FILED
July 20, 1990

No. 89-2773

SATURN DISTRIBUTION CORPORATION, a Delaware Corporation

Plaintiff-Appellant

v.

DONALD E. WILLIAMS, Commissioner of the Department of Motor Vehicles, Commonwealth of Virginia; VIRGINIA AUTOMOBILE DEALERS ASSOCIATION;

Defendants-Appellees

CENTER FOR PUBLIC RESOURCES, INC.

Amicus Curiae

On Petition for Rehearing with
Suggestion for Rehearing In Banc

The appellee's petition for rehearing and suggestion for rehearing in banc were submitted to this Court. In a requested poll of the Court, Judge Widener voted to rehear the case in banc; and Judges Ervin, Russell, Hall, Phillips, Murnaghan, Sprouse, Chapman, Wilkinson and Wilkins voted against rehearing the case in banc. As a majority of the Judges voted to deny rehearing in banc, and

As the panel considered the petition for rehearing and is of the opinion that it should be denied,

IT IS ADJUDGED and ORDERED that the petition for rehearing and suggestion for rehearing in banc are denied.

Entered at the direction of Judge Chapman with the concurrence of Judge Wilkinson. Judge Widener dissents. He would grant rehearing for the reasons expressed in his dissenting opinion.

For the Court,
JOHN M. GREACEN
CLERK

Appendix D

CONSTITUTION OF THE UNITED STATES

ARTICLE VI

Clause 2.

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

Appendix E

9 USC § 2

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

Appendix F

15 USC § 1222

An automobile dealer may bring suit against any automobile manufacturer engaged in commerce, in any district court of the United States in the district in which said manufacturer resides, or is found, or has an agent, without respect to the amount in controversy, and shall recover the damages by him sustained and the cost of suit by reason of the failure of said automobile manufacturer from and after August 8, 1956 to act in good faith in performing or complying with any of the terms or provisions of the franchise, or in terminating, canceling, or not renewing the franchise with said dealer: *Provided*, That in any such suit the manufacturer shall not be barred from asserting in defense of any such action the failure of the dealer to act in good faith.

Appendix G

15 USC § 1225

This chapter shall not invalidate any provision of the laws of any State except insofar as there is a direct conflict between an express provision of this chapter and an express provision of State law which can not be reconciled.

Appendix H

CODE OF VIRGINIA § 46.1-550.5:24.

On or before July 1, 1975, each motor vehicle manufacturer, factory branch, distributor, distributor branch, or subsidiary thereof shall file with the Commissioner a true copy of each basic form of franchise or sales agreement then in effect with motor vehicle dealers in Virginia, and thereafter shall file with the Commissioner a true copy of each new or different form of franchise or sales agreement thereafter offered to a motor vehicle dealer or prospective motor vehicle dealer in this Commonwealth no later than sixty days prior to the date such franchise or sales agreement is offered, provided that in no event shall a new or different form of franchise or sales agreement be offered a motor vehicle dealer in this Commonwealth until the form has been approved by the Commissioner as not containing terms inconsistent with the provisions of this chapter.

Appendix I

CODE OF VIRGINIA § 46.1-550.5:27.

It is unlawful for any manufacturer, factory branch distributor or distributor branch, or any field representative, officer, agent or any representative whatsoever of any of them:

10. To fail to include in any franchise with a motor vehicle dealer the following language: "If any provision herein contravenes the valid laws or regulations of any state or other jurisdiction wherein this agreement is to be performed, or denies access to the procedures, forums, or remedies provided for by such laws or regulations, such provision shall be deemed to be modified to conform to such laws or regulations, and all other terms and provisions shall remain in full force and effect," or words to that effect.